

## William White on the next recession January-February 2016

### [World faces wave of epic debt defaults, fears central bank veteran](#)

Situation worse than it was in 2007, says chairman of the OECD's review committee  
Ambrose Evans-Pritchard, The Telegraph, January 19, 2016

The next task awaiting the global authorities is how to manage debt write-offs without setting off a political storm. The global financial system has become dangerously unstable and faces an avalanche of bankruptcies that will test social and political stability, a leading monetary theorist has warned.

"The situation is worse than it was in 2007. Our macroeconomic ammunition to fight downturns is essentially all used up," said William White, the Swiss-based chairman of the OECD's review committee and former chief economist of the [Bank for International Settlements](#) (BIS).



"Emerging markets were part of the solution after the Lehman crisis. Now they are part of the problem, too." "Debts have continued to build up over the last eight years and they have reached such levels in every part of the world that they have become a potent cause for mischief," he said. "It will become obvious in the next recession that many of these debts will never be serviced or repaid, and this will be uncomfortable for a lot of people who think they own assets that are worth something," he told The Telegraph on the eve of the World Economic Forum in [Davos](#).

"The only question is whether we are able to look reality in the eye and face what is coming in an orderly fashion, or whether it will be disorderly. Debt jubilees have been going on for 5,000 years, as far back as the Sumerians." The next task awaiting the global authorities is how to manage debt write-offs - and therefore a massive reordering of winners and losers in society - without setting off a political storm.

Mr White said Europe's creditors are likely to face some of the biggest haircuts. European banks have already admitted to \$1 trillion of non-performing loans: they are heavily exposed to emerging markets and are almost certainly rolling over further bad debts that have never been disclosed.

The European banking system may have to be recapitalized on a scale yet unimagined, and new "bail-in" rules mean that any deposit holder above the guarantee of €100,000 will have to help pay for it. The warnings have special resonance since Mr White was one of the very few voices in the central banking fraternity who stated loudly and clearly between 2005 and 2008 that Western finance was riding for a fall, and that the global economy was susceptible to a violent crisis.

Mr White said stimulus from quantitative easing and zero rates by the big central banks after the [Lehman crisis](#) leaked out across east Asia and emerging markets, stoking credit bubbles and a surge in dollar borrowing that was hard to control in a world of free capital flows. The result is that these countries have now been drawn into the morass as well. Combined public and private debt has surged to all-time highs to 185pc of GDP in emerging markets and to 265pc of GDP in the OECD club, both up by 35 percentage points since the top of the last credit cycle in 2007.

"Emerging markets were part of the solution after the Lehman crisis. Now they are part of the problem too," Mr White said. Mr White, who also chief author of G30's recent report on the post-crisis future of central banking, said it is impossible know what the trigger will be

for the next crisis since the global system has lost its anchor and is inherently prone to breakdown. A [Chinese devaluation](#) clearly has the potential to metastasize. "Every major country is engaged in currency wars even though they insist that QE has nothing to do with competitive depreciation. They have all been playing the game except for China - so far - and it is a zero-sum game. China could really up the ante."

Mr White said QE and easy money policies by the US Federal Reserve and its peers have had the effect of bringing spending forward from the future in what is known as "inter-temporal smoothing". It becomes a toxic addiction over time and ultimately loses traction. In the end, the future catches up with you. "By definition, this means you cannot spend the money tomorrow," he said.

A reflex of "asymmetry" began when the Fed injected too much stimulus to prevent a purge after the 1987 crash. The authorities have since allowed each boom to run its course - thinking they could safely clean up later - while responding to each shock with alacrity. The BIS critique is that this has led to a perpetual easing bias, with interest rates falling ever further below their "Wicksellian natural rate" with each credit cycle.

The error was compounded in the 1990s when China and eastern Europe suddenly joined the global economy, flooding the world with cheap exports in a "positive supply shock". Falling prices of manufactured goods masked the rampant asset inflation that was building up. "Policy makers were seduced into inaction by a set of comforting beliefs, all of which we now see were false. They believed that if inflation was under control, all was well," he said.

In retrospect, central banks should have let the benign deflation of this (temporary) phase of globalisation run its course. By stoking debt bubbles, they have instead incubated what may prove to be a more malign variant, a classic 1930s-style "Fisherite" debt-deflation.

Mr White said the Fed is now in a horrible quandary as it tries to extract itself from QE and right the ship again. "It is a debt trap. Things are so bad that there is no right answer. If they raise rates it'll be nasty. If they don't raise rates, it just makes matters worse," he said.

There is no easy way out of this tangle. But Mr White said it would be a good start for governments to stop depending on central banks to do their dirty work. They should return to fiscal primacy - call it Keynesian, if you wish - and launch an investment blitz on infrastructure that pays for itself through higher growth.

"It was always dangerous to rely on central banks to sort out a solvency problem when all they can do is tackle liquidity problems. It is a recipe for disorder, and now we are hitting the limit," he said.

Financial apocalypse

[Ex BIS chief economist William White warns of epic debt tsunami worse than 2007](#)

International Business Times, January 20, 2016

Global debts have built up to such an extent that the world is facing another financial crash, worse than the one in 2007-08, according to a leading monetary theorist. William White, the chair of the Organisation for Economic Co-operation and Development (OECD)'s review committee, has added to former 'doomsday prophecies' by financial analysts, saying that the world has to look "reality in the eye" about the economic situation.

Ahead of the World Economic Forum at Davos, White underlined the significance of the crisis in China for the world economy. "Emerging markets were part of the solution after the Lehman crisis. Now they are part of the problem too," he said.

The situation is worse than it was in 2007. Our macroeconomic ammunition to fight downturns is essentially all used up.

White, the former chief economist at Switzerland-based Bank for International Settlements, raises concerns over the global economy after the Royal Bank of Scotland's credit team [issued a "sell everything" statement](#), warning of plunging stocks and an oil price of \$16 (£11, €15) a barrel in 2016.

"Debts have continued to build up over the last eight years and they have reached such levels in every part of the world that they have become a potent cause for mischief," White [told the Telegraph](#). "It will become obvious in the next recession that many of these debts will never be serviced or repaid, and this will be uncomfortable for a lot of people who think they own assets that are worth something."

These debts will result in Europe's creditors receiving the worst blow, according to the economist. With an estimated \$1tn outstanding bad loans by European banks, the continent is [increasingly vulnerable to China's performance](#). "The situation is worse than it was in 2007. Our macroeconomic ammunition to fight downturns is essentially all used up," White said. "The only question is whether we are able to look reality in the eye and face what is coming in an orderly fashion, or whether it will be disorderly."

#### Chinese impact

The doomsday predictions by various analysts come as the world keeps a close eye on China, which seems to be busting the myth of the everlasting emerging market. In January, Chinese authorities confirmed what markets were long fearing. The country's economic growth hit a 25-year-low, at 6.9%, according to official figures. Analysts looking at proxy-data such as energy usage and demand for electricity fear this number is in reality closer to 4% growth. A Nikkei report in 2015 estimated China's economy was growing 5% annually.

The slowdown in China has weighed on commodity prices as well. A global oversupply is not being met by demand anymore, as the country's manufacturing sector is slowing down and therefore needs fewer commodities. This, in turn, is affecting commodity depending markets as well. In September 2015, for example, Standard and Poor's gave Brazil's credit status a "junk" rating. The country's export value more than doubled since 2005 to \$256bn and accounts for around 14% of Brazil's GDP. When exports fall, so does the country's economy.

"Like many other countries, including South Africa, Canada and Australia, Brazil is suffering from what is going on in commodities and, of course, also in oil," Sanjiv Shah, chief investment officer at Sun Global Investments, told IBTimes UK. "These prices have fallen hugely, with oil being worth half the price per barrel that it was a year ago."

Not everyone is as negative on the economic developments, however. Business tycoon Martin Sorrell said in August 2015, shortly after the first stockmarket crash in Shanghai that he considers himself "a raging bull in relation to China". "China has been the biggest driver of the world economy," he told the BBC's Today programme. "They ain't done too bad with a five-year planned economy since 1985."

#### [Central Banks Make Global Economy Vulnerable, OECD's White Says](#)

Maria Tadeo, Bloomberg, February 9, 2016

Central banks' ultra-loose monetary policy is putting the world economy at risk, said William White, a senior adviser to the Organization for Economic Cooperation and Development. Negative interest rates and quantitative-easing programs from the U.S. to Japan may have unintended side effects such as higher debt levels for both sovereigns and

consumers, said White, who leads the OECD's Economic and Development Review Committee. Central bankers have been dragged away from their focus on inflation as governments struggle to generate sustainable growth, he added.

"The objective of that policy has changed totally -- it's trying to stimulate aggregate demand and the honest truth is that it's not capable of doing that in a sustainable way," White said in Bloomberg Television interview on Tuesday. "If people thought we were in a period of deleveraging that would set the scene for a period of robust growth. We haven't even started yet."

Investors are looking for European Central Bank President Mario Draghi to ease policy in the euro area further as early as March as the slump in oil drags down inflation while the Bank of England has dialed back talk of increasing rates and bets on the Fed hiking again are retreating. Japan's 10-year bond yields fell below zero for the first time ever on Tuesday after the central bank imposed negative interest rates on bank reserves.

White said he is "skeptical" about the benefits of such moves because of the strain they put on the banking system. "Negative rates on reserves are actually squeezing bank profits, and this is something we don't want in these circumstances, we want them to build up their capital buffers," he said. "This is all experimental." White said that the global economy needs those governments with budget leeway to boost spending and said policy makers should pay more attention to wage growth, which remains "too low." He said governments also need to make further structural reforms to boost growth and take a more systematic approach to debt reduction.

### [OECD's William White: In Terms of Debt, the Situation Is Way Worse than 2007](#)

financialsense, February 24, 2016

William White, chairman of the Economic and Development Review Committee at the OECD and former chief economist at the Bank for International Settlements (BIS), says the risks posed by global debt levels are greater today than they were in 2007 and that central banking monetary policy has lost its effectiveness. He also explains the crucial differences between modern macroeconomic modeling and complexity theory (or viewing the economy as a complex adaptive system) and the key lessons this has for policymakers, both fiscal and monetary. Here's a portion of his recent interview with Financial Sense:

"If you think about a crisis period as a period of deleveraging, in fact this has not happened and we've gone in the very opposite direction. Now, on the household side, clearly there have been some improvements made but on the corporate side in the US, things have gotten significantly worse—the debt ratios for corporations have gone up very substantially as has government debt...

More importantly—again, when I say the situation is worse today than it was in 2007—in 2007 this debt problem was essentially confined to the advanced market economies. Since then, the debt ratios—the private debt ratios in particular—have exploded in the emerging market countries and so we now have in a sense a global problem whereas in 2007 you might say we had a regional problem with the advanced market economies. But now it's basically everywhere so, yes, I do think that the situation is worse than it was then... When I first came to the BIS in 1994, we started warning about the credit flows into Southeast Asia well before the Asian crisis happened and...it was in the early 2000s that we really started to focus on what was going on in the advanced market economies... The story that we were telling then was really one of the Greenspan put starting in 1987 and every time there was a problem, the answer was to print the money or ease monetary conditions and the debt ratios ratcheted up and up and up...

So we had this problem in '87 and the answer was easy money; then we had this problem in 1990-1991 and, again, the answer was easy money. The response to the Southeast Asian crisis was don't raise rates even though all sorts of other indicators said you should. Then it was easy money again in 2001 and, of course, in 2007...every time the headwinds of debt have been getting higher and higher and the monetary easing required to overcome that has had to get greater and greater and the logic of that takes you to the point where you say, well, in the end monetary easing is not going to work at all and...that's where I am today... Unfortunately, we are still, as far as I can tell, both the BIS and myself are still talking to a brick wall...

There are a lot of reforms that could be carried out that in the fullness of time would increase growth, increase potential, and increase the capacity to service debt so there's a lot of things that might be done but it all starts off with a recognition, which we do not have, that monetary policy is not the solution to this particular problem and that it may, in fact, be making it worse. To put it in a nutshell, if it's a debt problem we face and a problem of insolvency, it cannot be solved by central banks through simply printing the money. We can deal with illiquidity problems but the central banks can't deal with insolvency problems...

In a way, I think the economists have made what the philosophers would call a profound ontological error. They have assumed that the economy is understandable and they have therefore assumed that if they can understand it they can control it.

And I guess the point is—and this is the ontological error—what you can understand about a system depends upon its nature and the nature of the economy...and all the interactions between the real and the financial side are in constant change...constant evolution. Systems like that cannot be completely understood and they certainly can't be completely controlled so this is a fundamental mistake that I think the economists and modelers have made.

The difficulty with having made a mistake of that sort is that it leads you to do things that in the end prove to be just wrong. The difference is how do you tend a machine and how do you tend a forest? These are very different animals and they have a very different nature. And if you look at the economy as a complex adaptive system basically you end up with a bunch of assumptions about how it works that are absolutely at the opposite end of the spectrum of the assumptions made in modern macroeconomics...

Just the very fact that you embrace the concept of the economy being a complex adaptive system can lead you to some very simple but very important lessons. Lesson number one from all of these other areas of complexity, like traffic, crowd movements, spread of crime, social webs, mobility of disease and epidemics—this list goes on and on of these things...but if you embrace this then what you can do is go back to the basic lessons that have been learned from all of these other disciplines and say what does this teach us for economics? And lesson number one—and these are all very simple lessons—is these systems break down all the time and they break down according to a power law, which basically says you get a big breakdown very infrequently and you get little breakdowns all the time...

Lesson number two is that you can't predict when the system will break down precisely or where it will break down precisely but in a sense it doesn't matter because it's the system you want to focus on. And it is possible to get some sense of this system is getting stretched beyond its capacity to recover. And I think this is one of the central lessons of the BIS, which is the levels of credit—the stock of credit—and sometimes the rate of growth of that credit is of such a magnitude that it is clear that there's going to be some bad things that come out of it...which is what makes me so fearful about China..."