



PRESS RELEASE

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A full house at the Teatro Sociale for the last event of the 2009 Festival of Economics

MICHAEL SPENCE: THE IMPORTANCE OF EMERGING COUNTRIES

After the crisis, the scenario will be dominated by the dynamics of China and India

The closing session of the fourth Festival of Economics was entrusted to the 2001 Nobel prize-winner Michael Spence, introduced by the scientific coordinator of the event, Tito Boeri, in the magnificent setting of the Teatro Sociale. The session was dedicated to the post-crisis scenario in the medium to long-term, centring particularly on the role of emerging countries, China and India above all.

Boeri began by recalling some of the most important moments during this year's Festival, particularly the format of public trials – introduced for the first time – economists themselves having been brought to the dock. Boeri also underlined the vitality and capacity for self-criticism manifested by the category during a difficult festival, precisely because it coincided with the international economic crisis, and their openness to other disciplines, particularly psychology (as has taken place in the past with sociology).

Coming to Spence, Lecturer at Stanford University and Chairman of the Commission on Growth and Development, which is supported by the World Bank, Boeri recalled his fundamental contribution in the field of asymmetric information: essentially this theoretical approach explains how a product is "sold" (from investment funds to higher educational qualifications), launching reassuring signals to potential buyers (client, employer) in a climate of uncertainty which makes it difficult for the buyer to evaluate the best behaviour to adopt. However, Spence's theory also helps us to understand the origin of the crisis, its evolution and possible ways out. In Trento the Nobel prize-winner chose to talk above all about this: how to come out of the crisis and what behaviour the G20 should adopt in order to reduce global inequality. "The two things are closely related", reiterated Boeri.

Spence began by first of all briefly illustrating the origin of the crisis, developing within the American financial system. The system of regulating the financial markets in America and Britain has been completely discredited. The capital leaving advanced countries for

developing countries has also dried up, as a result of the credit crunch. Consumption has gone down and the effects have been felt in trade and hence once again by emerging countries.

When we re-emerge from the crisis, Spence stated that he was sure that the scenario will be different. There will be what he describes as a "new normal", while the financial sector will be much more strictly regulated, perhaps even too much, the margins of reserve will be higher, the cost of capital greater and overall, as a result of all these variables, growth will be slightly lower. Greater resources will be destined for savings (those in American families had stood at zero). It will thus be necessary to do something to make up for the deficit in demand. "If Americans have to tighten their belts, it could be developing countries, which saved more in the past, that spend more. The Chinese for example are known for their high level of savings. On the other hand, if we do not succeed in making up for the deficit in demand it is likely that countries will tend to adopt protectionism, in order to retain their own demand internally and exclude external competitors."

What is the long-term scenario in view of the crisis? In the last 30 years the world economy has changed spectacularly. 30 years ago only 16% of the population lived in developed countries, whereas most people lived in poor countries. The spectacular growth of China and India has meant that today 60% of the world's population lives in advanced countries or countries with a very high growth rate. Around the middle of the century – unless absolutely exceptional events occur – around two thirds of the world will live in "advanced" environments, not only as regards income but also in relation to energy consumption and other factors.

One of the effects of these epoch-making changes is that the G20 is taking over from the G7 in terms of coordinating global economic development. Overall these 20 countries represent 90% of world GDP. With current growth rates, in the next few decades India and China together will surpass the USA and the EU in absolute terms, while subsequently China will surpass these competitors on its own.

So what about the countries outside the G20? These 120 countries are poor and in many ways impotent with regard to the current crisis. They do not have reserves and they are unable to stabilise their currencies. However they are important: new problems will inevitably arise if one third of people globally are excluded from the growth in the world economy. Ultimately the G20 countries have one historic mission above all: to help and support all the others. This must take place in many fields: if food prices increase suddenly, as happened last year, many people will die of hunger; if the impact of climate change is in line with the worst forecasts, it will be necessary to help those who live in less developed countries to defend themselves from the worst effects (flooding, famine, drought etc.).

To return to China and India: here there has been an enormous fall in poverty starting from the 1970s and 1980s, although India still has a long way to go. China has seen an enormous reduction in overall poverty but a much more substantial growth in high incomes: there is now similar inequality to that existing in the USA. There has also been a drop in the rural population and very rapid urbanisation (more rapid in China than in India).

The financial crisis has also had an impact on these countries, but it is likely that they will

be the first to recover. According to some forecasts, by the end of 2009 China and India will experience a growth of 8-10 %, whereas the advanced economies will only begin to grow again in 2010.

On the other hand, Asiatic countries continue to have difficult relations with the IMF, due to the authoritative attitude that the Fund has adopted in the past. We will see how the situation will evolve in the future.

However, in general global growth will be driven by the more dynamic developing countries, although these will not substitute western countries, which nevertheless have 65% of the GDP. There are also other dynamics to be considered: advanced countries are ageing, there are problems with their pension systems and also with extending working age to at least 70. At the same time there is imbalance between employment demand and offer, only partly made up for by migration flows. In the future we can expect widespread unemployment among young people and this is a big problem. The other major problem is: can the whole world consume in the same way we do, at the same levels, with the same emissions, without destroying the world? Probably not, bearing in mind the forecasts regarding climatic change. Advanced countries are asking China and India to cut their emissions, but they note how those most responsible for CO² emissions are the USA and Europe. It is reasonable to suppose that industrialised countries will have to lower their emissions, whereas developing countries will increase them. It will therefore be necessary to concentrate more on energy efficiency and it is certain that this will be one of the fundamental items on the agenda for the next 10 years.