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The Global Financial System Was Better Prepared for the Pandemic Than 2008

Guests:
For the Motion: Jason Furman
Against the Motion: Gillian Tett
Moderator: John Donvan

AUDIENCE RESULTS	
Before the debate:	**After the debate:**
43% FOR	**50% FOR**
31% AGAINST	**40% AGAINST**
26% UNDECIDED	**10% UNDECIDED**

Start Time: (00:00:00)

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John Donvan:
This is Intelligence Squared U.S. and welcome to our first debate done digitally. The setting is virtual, but the arguments are real and so is your moderator, me John Donvan. And as we see right now all around us an economic ice age, this shut down in human activity that's been ordered and organized by governments to slow the spread of the coronavirus we are also seeing a series of specific industries stressed possibly to the breaking point. Airlines especially, but also travel in general; big swathes of the food industry, but especially restaurants; professional sports, but also all entertainment that depended on getting large numbers of people together in one place. But the industry we're going to be taking a close look at is the one that gets summed up this way: the global financial system. And it's interesting to us because the last time the economy was anything under the kind of stress that it is right now was back in 2008 during the global financial crisis when that system came this close to a total crash.

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So what we're going to be asking is how is that system working now in the pandemic; is it headed for collapse as a result of potential widespread bankruptcies and unpaid loans and markets bereft of participants. Or will the global financial system be able to withstand whatever may come in the pandemic thanks to lessons that were learned and reforms that were undertaken after the global financial crisis of 12 years ago? Well in those questions we think we think we have the makings of a debate, so let's have it.

Yes or no to this statement: the global financial system was better prepared for the pandemic than it was for 2008. I'm in Washington, D.C. Our two debaters are joining me from New York City and from Cambridge, Massachusetts. We are recording on Wednesday, April 29th 2020. As always, our debate will go in three rounds and then you, our at-home audience, will be choosing the winner. You're going to be asked to cast two votes. One before you hear the arguments, and that's going to take place in just a second, and then another after the debaters have made their cases.

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The side that sways the most mind will be our winners. So let's go to your first vote, and you can do this from any browser. You can do it on your laptop, or on your phone, or on a tablet. Go to iq2us.org/vote. That's I-Q, the number two, U.S. dot org forward slash vote. And there you can ask your vote for, against, or undecided on the resolution which again is: the global financial system was better prepared for the pandemic than for 2008. We'll wait for you; go do it and then come back.

Now let's meet our debaters. Again, the resolution is this: the global financial system was better prepared for the pandemic than for 2008. And arguing for that resolution I want to say hello first to Jason Furman. Jason, welcome to Intelligence Squared U.S.

Jason Furman:
Great to be here.

John Donvan:
Jason, you've debated with us before, and you were one of President Obama's top economic advisors and you served as Chairman of the Council of Economic Advisors from 2013 to 2017.

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You're now at Harvard University; you're a professor of the Practice of Economic Policy and we just want to say it's great to have you. We love the way you debate and the way you present an argument. So thanks for joining us.

Jason Furman:
Just wish it was in person.

John Donvan:
[laughs] So do we, but this is the best we're going to do, and we're pleased to be doing it also with Gillian Tett; Gillian, welcome back to Intelligence Squared. You are at the Financial Times U.S. and Chair of the Editorial Board. You are -- we want to thank you for joining us. And I also want to put out there a little bit of background for those of you who didn't attend our previous iteration of this debate back in 2019 we debated on the resolution: 10 years after the global financial crisis the system is safer. We had Jason Furman and Neil Kashkari arguing for the resolution. Arguing against we had scheduled Gillian Tett and Kenneth Rogoff, except Gillian we missed you that evening during -- due to a flight mishap. So at the 11th hour, our Chairman Robert Rosenkranz took your seat and he argued in your place. We're actually going to hear from him a little later in the program. So we're sorry to have missed you then and as Jason said, we're sorry that it's not all in person now.

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But we are delighted to have you here and to have both of you making your cases for the side that you're on in this time of pandemic.

Gillian Tett:
Well it's great to be here, and one of the unexpected silver linings of this crisis is that we don't have planes to miss anymore.

John Donvan:
Well if we're going to call that a good thing [laughs] that sounds like as optimistic a spin on this that I can possible imagine. So let's move forward in that spirit, and let's move on to round one. Round one will be opening statements be each debater in turn. They will be four minutes each and up speaking first for the resolution: the global financial system was better prepared for the pandemic than it was in 2008, is the former Chairman of Economic Advisors Jason Furman. Jason, your time begins now.

Jason Furman:
Great, well it's great to be with all of you virtually. The novel coronavirus has created a massive human tragedy on a global scale. It's creating an economic tragedy on a global scale.

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I am very worried, not just about where the economy is today which is a deliberate result of the virus and the policies to contain the virus, but I'm also worried about where the economy we be one, two, or three years from now and what the recovery will look like. The proposition on this debate, though, is whether the global financial system was better prepared than it was in 2008 and I'm going to try to convince you that the answer to that is definitely yes. In fact, of all the shoes that have dropped, that one has not. Whether this pandemic struck us in 2020, or 2010, or 2000, or 1990, it would have been devastating for the economy. The devastation would have been compounded if it was impossible to respond economically using the main tools that the policymakers have, monetary and fiscal policy, and if it spread into a financial crisis which is something we know from history can be very severe and almost guarantees long lasting economic pain.

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One of the worries that people had recently as a few months ago was with fiscal policy. Would we have enough space to increase government spending or cut taxes if there was a crisis? Some people argued yes; some people argued no. The answer is now clearly yes. All of the advanced economies have had enough space to do massive amounts of increased spending, tax cuts of a scale that has not been seen since World War II.

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They've done that with interest rates that today are lower than where they were in 2009. In fact, today we are borrowing at negative real rates to finance that fiscal response, not the positive real rates we had then. A second concern is that we wouldn't have monetary policy, and yes, monetary policy has been constrained because we came into this with lower interest rates, but we learned a lot about how to conduct monetary policy in fighting the last crisis. And the Fed was very quick, as was the ECB, as have other central banks around world been very quick to move to that novel set of tools, sometimes called quantitative easing that have greatly expanded their balance sheets. And as a result, we haven't seen interest rates spreads, a measure of risk in markets, rise anything like they did in the last crisis. And in fact, some key interest rates like the interest rates on mortgages have actually come down.

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Finally and perhaps most importantly is the banking system. Banks are like the nerve system of an economy. If they start to fail, you don't get lending and people's money becomes unsafe, and history says that takes about a decade to recover from. We put in place much stricter rules on bank capital in the wake of the last crisis. And so banks went into this crisis holding larger buffers, about 50 -- about twice as high by one measure, 50 percent by another. Regulators had been doing stress tested regularly to understand just what a nightmare scenario would look like for the banking system, and so they basically looked at and prepared for a scenario along the lines of what we're seeing now.

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John Donvan:
Jason Furman --

Jason Furman:
And --

John Donvan:
-- I'm very sorry but you're time is up. You've hit your limit but you can continue your thoughts as go on, but thank you very much for your opening statement. And now that you have heard

Jason's argument for the resolution let's go to our second debater who will be arguing against again the resolution being: the global financial system was better prepared for the pandemic than we were in 2008. Here to make her opening statements, Gillian Tett, Editor at Large at the Financial Times U.S.

Gillian Tett:
Well thank you. Well, I'd like to start by saluting the incredible things that policymakers have done in the last few weeks which, as Jason has pointed out, are truly phenomenal and in many ways very brave, so well done. But, and there's always a but, we have to ask: why did policymakers need to take these extraordinarily extreme measures? It was partly because the severity of the economic shock, but it was also because of something else. We have not learned all the right lessons from the last financial crisis or cleaned up the system to put it on a safer footing ahead of the next one, i.e. this one.

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What do I mean by that? Well let's think about some of the things that caused the last financial crisis: debt. You'd think that after you'd had a debt-fueled financial crisis, you would then go about and try and cut debt. Think again. In the last decade, debt as a proportion of global GDP, has gone from 280 percent to 320 percent and it's likely to go even higher as a result of the current crisis. In fact, people are saying it could go to 360 percent. So we have way too much debt and that has made the financial system a lot more fragile. Secondly, think about shadow banking. The last crisis had a big problem in the shadow banking sector; so you'd think that for this crisis they would have actually cleaned up the shadow banking sector in the last decade, wrong. This time around the shadow banking sector's got even bigger, and we've already seen the brutal impact of that through things like hedge funds taking on way too much leverage in the treasuries market creating the very nasty market gyrations in March that regulators had to step in and try and deal with.

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Complexity. You'd think that after the last crisis caused by way to much complexity they would have come in and simplified the system and ensured we actually understood how all the new flashy financial innovations actually worked. Have they done that? No. This time around we not only have a whole bunch of new complex financial innovations which are not well understood, we also have the fact that electronic trading has taken over the markets to a degree that most regulators, and certainly most investors and politicians, do not understand what the robo-traders are doing. And that makes markets gyrate even more dramatically. And last but not least, contagion. Contagion means that we have to have a world where policymakers coordinate really closely. Now the good news is central bank governors are coordinating very closely, and there's incredible collaboration there.

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But the rest of the G20, forget about it. We've seen an incredible lack of leadership or coordination. So you take those four things together, and I would argue that the financial system was less well prepared than it could have been, it should have been. And frankly given what we knew about the 2008 crisis, it was in many ways less prepared as a system than before 2008.

And last but not least, there's two more points. Firstly, Jason said that there had been these fantastic stress tests in the system, and that's actually true. Again, I salute the regulators and people like him who've pushed for stress tests. The problem is though that they've only stress test for the last war, i.e. what would happen with a mortgage crisis, what would happen with a recession. They weren't looking at things like pandemics or trying to get imaginative about thinking about what could come next. And the worse problem of all, the thing that really upsets me about the current situation, is that because there's been so much debt, because interest rates have been so rock-bottom low, so many people in the system, including many mom and pop investors, have taken some crazy risks in the search for yield.
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And that's made the system even more fragile.

John Donvan:

Thank you, Gillian Tett. And that concludes round one of this Intelligence Squared U.S. debate, our opening statements. And now we move on to round two. And round two is where the debaters address one another directly and they take questions also from me. And soon, after a few minutes, we'll be taking questions from members of our audience that have been submitted in advance. But to go back to the arguments that we heard, the resolution being: the global financial system was better prepared for the pandemic than 2008, we've heard both debaters concede, not concede, but actually assert that we're in a terrible situation. As Jason put it we're facing a massive human tragedy, we're facing a massive economic tragedy. But he argues that on the resolution, looking specifically at whether the global financial system is in better shape now than it was in 2008 to handle a situation like this, he says indubitably so because of the reforms put in place, because of the development of novel tools.

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He concedes that interest rates are so low that there's not much room for the Fed to use that tool, but that quantitative easing is part of the solution. He says that the banks are much better capitalized than they were the last time around, and that bottom line if we were going through this coronavirus thing before 2008 we would be in much worst situation even than we are now. And the global financial system would not be holding up as well as it is. As he says, right now among all of the industries that are in trouble, this is the one where the other shoe has not dropped.

Gillian Tett has countered that argument first of all by congratulating the innovation of financial institutions around the world in trying to deal with this situation, taking note especially of the use of the quantitative easing tool that Jason was referring to. But she's saying that the fact that this tool has to be used, and used to such an enormous degree, resulting in increase in such debt itself is an indication that we're actually not better off.

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She refers to her concern that we don't really know what's going on for two reasons; and that is that a large part of the global financial system is beyond the reach of regulators. I think she said something in the neighborhood of 75 percent of the global financial system is not just banking but beyond, and unregulated. And also that so much is now done by algorithms and by computers that we really don't even know how well we're doing. So that she would challenge the very idea that we can assert that we're better off. So I want to take that point to Jason. Very, very specific point that Gillian made that because computers are so involved in making the split-second trading decisions et cetera that we're not really sure where we stand on this.

Jason Furman:

I mean, first of all we had an awful lot of algorithmic trading, you know, a decade ago.

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But more importantly, why has the stock market gone down? It's gone down because of the present discounted value of corporate earnings have gone down because people are expecting a prolonged economic problem. Sure every day sometime markets overshoot in one direction. Sometimes markets overshoot in the other direction, but the broad change in the stock market from February through now is roughly consistent with what you'd expect given that, you know, certain industries like airlines hit very hard. You know, other industries hit less hard and the like. And so it broadly looks to me like a roughly rational response. And it's a rational response to a massive, massive, massive economic shock, the largest in a century. And nothing can insulate us and insulate markets against a shock that big.

John Dovan:

Gillian, what's your response to Jason's point that he sees no sign that the algorithms are doing particularly irrational or unpredictable things?

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That they're reflecting a rough economic situation.

Gillian Tett:

Jason's completely correct. There are very good fundamental reasons for why markets have collapsed by 25, 30 percent because guess what? The economic outlook looks a lot worse. But here's the real issue: you've had this incredible about of validity and crazy gyrations much of which is due to the fact that the rise of electronic trading and robo-trading has changed the liquidity provision, i.e. how easy it is to actually trade or not. And what's worse than that is that, although you have ultra-sophisticated hedge funds who understand what's going on or you hope they understand it, you can bet your dottom bollar [sic] that they vast majority of retail investors have absolutely no idea, and no hope of understanding what the robots are up to. So if you want to create a system where essentially wider society buys into the stock market and capitalism, you need to have some sense they understand it rather than seeing ETF prices or stock prices go up by five percent one day, down by five percent the next, et cetera, et cetera.

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So for that reason, it's a very pernicious situation.

John Donvan:

So Jason, there's a question that Gillian put out there that I don't think she means in a rhetorical way; I think she means it as a challenge. What were regulators doing by allowing rates to stay so long? And doesn't that in itself constitute an enormous risk to the system that does not reflect the sense that we're better off after 2008?

Jason Furman:

Yeah, the main goal of policy prior to the crisis was to have low unemployment and stable inflation. And policymakers were quite good on unemployment; it was quite low in a lot of countries. Inflation was still below target, not above it. So I don't think monetary policy was too accommodative before this. And I think you risk getting, you know, overly focused on -- there were gyrations markets, a lot of which, by the way, are a month, a month and a half in the past and that we're not seeing on a continual basis now.

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And we're not seeing it on a continual basis now because the Fed, rather than having to invent brand new tools, could take out the same tools that it invented a decade ago, benefit from that learning, and keep interest rates for treasuries, for mortgages, for corporate debt, in a relatively unstable place. So yes, if you look at certain technical features of markets, especially in March, you'll see all sorts of gyrations. You step back and look at the big picture: rates remarkably low and stable, you know, financial systems remarkably stable, of course the equity market, as we both agree, is down. That reflects an underlying worse reality. But the place where regulators can affect things, credit markets, have behaved, broadly speaking, quite well.

John Donvan:

Gillian?

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Gillian Tett:

To my mind, one of the most pernicious aspects what's happened the last decade or 12 years, is that ultra-low interest rates and quantitative easing were initially introduced as a short-term, supposedly temporary measure which has become guess what, completely permanent. And that's had two or three impacts. One of them is that it's made it very hard to distinguish good companies from bad in the sense that everyone's being propped up. You have essentially zombie markets and zombie companies. Secondly though, you have a situation where lots and lots of investors, including most pension fund managers and mom and pop investors, all the people who we kind of count on to essentially manage our money for the future, they have been taking crazy risks, increasingly crazy risks, because interest rates have been so low. They've been forced to look for returns in all kinds of different places. And the entire system has slid into a situation where it's essentially structurally addicted to low rates and they take it for granted to a point where they suddenly reversed, there's going to be big losses.

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We're not seeing that right now but we certainly could do in the future. And the third problem is that by cutting rates so low already, the Federal Reserve and other central banks haven't got a lot of ammunition in their arsenal to fight a new crisis. So one of the reasons they're resorting to these crazily extraordinary measures right now is precisely because they don't actually have the option of using what they would have used before because they've already used it. So you add that together and that's a reason why low rates have created more fragility, not less, in the system.

I think a better way to look at what's going on right now, Jason, is that before 2008 you had a financial system that was addicted to private sector debt a bit like someone being addicted to heroin. And then you had a crisis and the central bank stepped in, and they weaned the system off the private sector debt, the financial heroin, or they rather atoned for the sudden disappearance of that by providing morphine in the form of central bank credit

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Quantitative easing, that's essentially what it is. And what you've seen in the last couple of months is essentially doubling down on that. Because when corporate bond prices, for example, started to collapse which means that cost of borrowing for companies started to go up, what did the central bank do? It stepped in and said it would buy corporate bonds and essentially support the market. So essentially you've had a situation where you've come out of the last crisis even more addicted to morphine. And so the big question that hangs over the entire system, which nobody has an answer to at the moment, is what will happen if that supply of morphine, central bank support, ever dries up? I mean, maybe you can say, Jason, doesn't need to worry about that because guess what? It's going to always be there. Central banks will just keep supplying more and more and more morphine and essentially doubling down all the time. But what I'm concerned about is that you've bought peace today at the cost of a lot more uncertainty and risk in the future.

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John Donvan:

Jason do -- so Gillian's made this point a couple of times, that the fact that we had to see central banks scrambling through March and into April in itself -- like really scrambling, like massively unprecedented kind of responses, in itself, suggests that we're not better off. That these are -- that it's the equivalent of coming up with a new way to put out a fire because the old way didn't work. And I just want to get your response to that kind of bar that she's setting in making her argument.

Jason Furman.

Yeah. The unemployment rate today might be higher than the unemployment rate was in the Great Depression. The economy has never ever, ever had the type of negative growth rates that we're going to see in the second quarter of this year. Of course the Fed had to do a huge amount. The people like Gillian who are arguing that this was morphine and addictive and a problem were making the argument that what happens if we get into a crisis?

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We won't have any tools left, we won't be able to do any more of this, we won't be able to respond. I'm not saying Gillian was making all this arguments, but a lot of people were saying, you know, because of everything the Fed is doing, when we get into a real crisis they won't have any room left to respond. Well they have proven that completely wrong; they have had room to respond, and they have responded very effectively taking something that in some ways is even worse than the Great Depression so far and made it so that you barely even notice what was going on in credit markets if you weren't watching obsessively day-to-day. But big picture, you know, functioning perfectly fine.

Gillian Tett:

Well Jason, I take your point but the reality is the Fed has bought peace today, or a modicum of peace, at extraordinary cost for the future. Because it's come in, it's provided all this cheap credit, all this cheap money, which essentially is propping up companies which may yet go bust.

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In which case somebody is going to have to pay the price for that and take the losses. It's essentially meant that anyone who is a saver can't get any return going forward because, with rates ultra-low almost indefinitely, there won't be the normal kind of returns that so many savers depend on. And it's also doing all this at the potential cost of threatening the central bank's own credibility. Because where we are heading now is essentially about the central bank buying government debt directly; underwriting the operations of the government quite directly and that is something which could end up essentially leaving the central bank simply as a tool of the government. And if at any point people started to doubt the ability of America or the government to pay back that debt, doubt the ability that the central bank's actually independent enough to keep inflation low, then you could start to see a real financial crisis where people flee the treasury bond market, the government bond market, interest rates go spiraling up, the currency collapses, and you have a really nasty mess.

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That is not theoretical; we've seen that story play out a lot of times in other emerging markets. We've not seen it happen in America because people trust America right now, but where we're heading with this kind of combination of extreme measures could potentially be towards that kind of picture some way down the road.

John Donvan:

So Jason, what I heard from Gillian is a framing that’s somewhat -- a little bit different from yours. You're saying so far, the system has held up. And Gillian is saying so far isn't enough of an answer because this is an unfolding situation and that the seeds are sown for financial global system disaster, or breakdown, or seize up. That we're so not out of this that you wouldn't -- you shouldn't be calling this better than 2008.

Jason Furman:

First of all, are you asking me if the system is going to be perfect for the next several years?

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I'm certainly not going to argue that. If we are in the same economic position we are right now for the next year, we're going to have lots of problems in our financial system. That also would have been true, by the way, if you had shut down economic activity in 2008 or 1998, or 1978. I think that we are in better shape though because we came into this with low unemployment, with a somewhat higher inflation rate. And had the central bank not being doing what it was doing over the last decade, we would have had economic problems even before this shock hit us. So definitely no one can protect the economy fully against the consequences of this; it can't even protect the financial system against it. But the fact that we knew the tools we used, were able to roll them out very quickly, roll them out on scale, I think means that we're going to be handling it a bit better than we would have had it come earlier.

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John Donvan:

Gillian, do you concede the part of Jason's argument where -- I understand that you're making the argument that the system globally is bigger than banking, but he's saying the banking portion of the system is in much better shape than it was in 2008. Do you concede that point?

Gillian Tett:

Jason, or John, I completely concede the point that the banking system is healthier than it was in 2008, at least in America, in the sense that there's now much bigger capital buffers, dramatically bigger capital buffers, sort of rainy day reserves to protect banks against unforeseen losses in America. That's not the case in Europe to the same degree and unfortunately that's one reason that the European crisis could be worse, but in America that's true. And in addition to that, many senior bankers have overhauled their risk management strategies and done stress tests to make sure the system is stronger.

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The problem though is what's happening outside the banks in the so-called shadow banks, because hedge funds, ETFs, mutual funds, all these areas have been building up a lot more risk. Proud equity funds to, in terms of their credit operations. And that is very poorly understood, and that creates a different type of systemic risk in the capital markets. Because that's really where a lot of the risky activity is being transferred in the last decade; so what regulators should have been doing in the last decade or so, in addition to strengthen the banks, is imposing much stronger oversight on the shadow banks, much stricter rules. And if they'd done that, to cite one example, they wouldn't have been shocked when in the middle of March the U.S. treasuries market started to seize up. Because suddenly people discovered that hedge funds had taken up massive risks in the treasuries market with a large amount of borrowing that no one knew about before.

John Donvan:

All right, I'd like to move on to some audience questions. And we reached out to some of our most engaged audience members and boy did they have questions.

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So we're going to get to them in just a second, but first I wanted to go to a special questioner and that's our Chairman. The Chairman of Intelligence Squared, Robert Rosenkranz who argued, as I said earlier, in a debate in 2019 on whether 10 years after the financial crisis we were better prepared or not. He argued against the resolution at that point. But Bob, welcome to our first virtual debate.

Robert Rosenkranz:

Hi John, it's a real pleasure for me to be here at our first virtual debate. I'd like to welcome back Jason Furman who debated this topic previously, and especially Gillian Tett who was scheduled to do it previously and for whom I had to fill in at the last moment. In our previous take on this debate, I argued that the financial system was less prepared to deal with a crisis than it was back in 2008 and I've actually changed my mind about that.

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The main reason I've changed my mind is that the principle argument, or at least one of the principle arguments that I advanced, was the notion that governments were simply going to be less capable of reacting to a crisis. I felt that the executive of the U.S. government was less well staffed than it was then. I felt that Congress was more paralyzed by partisanship than it was then. I felt that U.S. global leadership was substantially diminished, and therefore it would be very hard to coordinate a global response to a global economic challenge. And I have to admit, I have been pleasantly surprised on all of those fronts. The government has stepped up with a huge stimulus package, some $2 trillion covering all manner of rescue for vulnerable segments of the economy. The Fed has expanded its balance sheet enormously.

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And there has been a degree of international coordination, if not conscience, at least that the major economies of the world have all converged on very similar policies of very accommodative monetary policy, central banks driving interest rates around the world to zero, making abundant capital available to keep the markets liquid, and all of that has happened in a -- at a time pace and a magnitude that far exceeds what we saw in '08-'09. So I really feel like the global governmental response to this has been far better than I would have anticipated.

This is a question for Gillian Tett. So you've posited that one of the big risk factors in today's world is the amount of debt outstanding which is greater than it was, obviously, going into the '08-'09 crisis.

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U.S. government debt is now close to 100 percent of GNP and will be well over 100 percent of GNP as next year plays out. But Japan, for example, has government debt around 250 percent of

GNP and it is pretty steadily been able to increase GNP on a per capita basis for decades now. So where is the evidence that current levels of debt are indeed dangerous?

Gillian Tett:

Well we certainly are likely to see many years of low or stagnate growth as a result of the debt burden, and I would suspect that the response of the authorities over time will be what we will call financial repression. That's essentially a concept pioneered by people like Carmen Reinhart that argues that the most effective way to reduce debt, which was used after World War II, is to engineer a situation where for many, many years interest rates are held below inflation.

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And that essentially means that anyone holding bonds ends up subsidizing the government and helping them to pay down the debt. So you can do that, but it takes a long time. And the reason why Japan has been able to weather its high debt burden, and the fact that its growth has not been particularly vibrant, is because it has a really strong sense of social cohesion and shared pain. And the question we have to ask ourselves, if we look at the western Anglo-Saxon economies as they move into a world with this absolutely astonishing level of debt we've not seen since World War II, do they have the social cohesion to actually engineer a smooth reduction in debt over time? Are we going to have dramatic financial duration?

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Are we going to have social explosions, or even create [unintelligible]

debt [unintelligible] default? None of those last potential outcomes are good for the financial system or, as it happens, for the economy.

John Donvan:

What's your take on that, Jason? You know, Gillian's arguing that Japan had advantages in being able to bring the debt back down and GNP up relative to population that we don't have, and there in again lie the seeds of disaster in the kind of responses that are happening right now. What's your response to that?

Jason Furman:

Yeah, I think the fiscal crisis and the debt crisis is the single most predicted economic crisis we've had. It's been predicted over and over and over again, and a lot of the people predicting it said, you know, if we have a crisis we won't be able to borrow to get out of it. Well look where interest rates are right now; look at our ability to borrow to deal with this, it's quite large.

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So I think people have massively overstated the evidence for the impact of debt in causing crises, massively overstated the evidence for it being a large negative for economic growth. That evidence is barely there. There's no evidence for a threshold that you cross over and all of a sudden it becomes a problem. And the final thing, I'd say, is there's a little bit of contradiction in the argument Gillian is making, because if we had had less of this debt then interest rates would have been even lower than what they were. So I think you can't simultaneously condemn the Fed and other central banks for low interest rates and have a policy prescription whose main effect would be that interest rates would be a lot lower.

Gillian Tett:

Well it's not just about government debt. I mean, I actually disagree on the point about the government debt.

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Because you could have actually had, you know, a policy where the Fed raised rates and it wasn't just due to market investment pressures that kept rates low; it's also due to the Fed's stance as well. But it's also in the corporate world. It you look at the crazy degree to which investors have been reaching for yields all over the place, the degree to which the private equity industry has been pumping up its activities, or simply the fact that, you know, corporate America has become significantly more leveraged in the last few years because money has been so cheap. All of that adds up to conditions which make you less well prepared for a crisis; go back to the original point of the discussion. And it's not where you'd want to be if you'd actually learned the lessons from last time around and you got better prepared for the pandemic, or shock.

John Donvan:

I'm going to go to a question now also sent in by a former -- another one of our former debaters actually.

00:38:02

And I want to say hi and welcome to Intelligence Squared, Allison Trager from New York.

Allison Trager:

Hi, I'm Allison, and my question is for the for side. And that is: if the financial system was so well prepared, why does the corporate bond market need so much liquidity now from the Fed?

Jason Furman:

Because the United States and the global economy is going through the worse thing it's gone through in a century, and that's what you have central banks for. Central banks are the lenders of last resort. Governments are the borrowers of last resort. When no one knows how deep this is going to go, how long this can last, even if you had superb credit going into this it's going to be a bit harder for you to borrow. And so that's why we have lenders of last resort. They are there for floods; there is a massive flood right now. They are doing what they do in that flood and, you know, it's working.

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And as a result, the second shoe of a financial crisis has not dropped to compound the first shoe that dropped very, very far, which was the virus itself.

John Donvan:

And Gillian, I'm assuming you're sympathetic to the tone of that question which really was a challenge to Jason. Do you want to comment on it?

Gillian Tett:

I think the question speaks for itself. You know --

John Donvan:

Okay.

Gillian Tett:

The banks have not jumped in to buy corporate credit on this scale before in America, and the fact that they had to jump in shows that actually the underlying dynamics of the corporate bond market, the particularly leveraged finance markets, the risky credit, we're not stable. And to go back to the key point, they were not where they want to be to repair for a pandemic.

John Donvan:

All right, we have a question now from Caitlyn in Vermont. And Caitlyn says, "it seems we are more politically polarized than we were in 2008, and the U.S. is not taking a global leadership position. Given the rise of populist economic policies and America first, can we really say that we were better prepared in 2020 for coronavirus?"

00:40:07

And Gillian, that goes to a point that you were beginning to develop in your argument, so I'd like you to take that question on first, the politics behind the situation.

Gillian Tett:

Absolutely. I mean, one of the problems is that to get out of a crisis like this you're going to have to make very hard choices about how you spread the pain. Because the reality is there's going to be pain, however you structure it. And you can either collectively decide how to spread the pain in a very egalitarian way that ensures that everyone's going to buy in, or you can simply force weak people to take the pain, or you get a revolution and force, you know, wealthy people to take the pain. But it does concern me that America doesn't have currently a mechanism for smoothly and fairly spreading pain that will get buy-in.

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And it's going to be a question that's going to haunt American for many, many years, because it's not just about who's going to cope with the potential loss of economic activity today and the potential defaults from the shutdown. It's what's going to happen in five years' time when people are starting to try and pay down their debt.

John Donvan:

Jason, I want to take that question also to you and also add this layer to it. The America first message also is very, very likely alienating and has been alienating to our traditional allies and even financially important rivals like China. And in a situation like this where you want to have some sort of global cooperation, are we in an era where we are better off to make the global financial system work in a cooperative way than we were in 2008?

Jason Furman:

Yeah, I think the answer to that is mixed, frankly. In some respects we're better off. The IMF had $250 billion capacity for lending back then, now it has $1 trillion capacity for lending.

00:42:04

The 1 trillion, by the way, is not enough. I think they're going to get $2.5 trillion of requests, but at least we've built up the IMF and the United States has continued to work with them. You know, obviously the United States is not working very cooperatively with the WHO and they're an organization that's more important, not just for health, but also for the economy as well than the IMF. And political polarization has effected, you know, the way even people read the facts on the extent of the virus, the dangers of it spreading, and how it should be responded to. So I think that political polarization has gotten in the way of our response. On the economic side, not so badly that we didn't move more quickly than we ever have in history to do something larger than we've ever done in history to deal with an economic crisis, which was the Cares Act. And the Fed I think has been outstandingly professional.

00:43:00

But certainly I wish we had, you know, a more competent and less polarized and more globally oriented political system right now.

John Donvan:

And Gillian, we have a question from Boulder, Colorado, James Mason, that takes the conversation we were just having a step further. Let's go to that question.

James Mason:

In last year's related debate, I thought the best argument against the motion was that the financial system is more interdependent now than it was, and as such, it's more sensitive. But I was convinced by the rebuttal that we know have more tools and regulations than we did, even if it's not everything that we want or should have. So my question is, over the last decade, was the rate of interdependency increased higher than the generation rate of new tools and regulations?

Gillian Tett:

Well that is a great question because in many ways what we're now living with is the contagion effect.

00:44:01

And the fact that ideas and germs and financial panics can flash around the world much faster than we can understand or know how to respond, and the real tragedy of the world today is that most of the big problems that we face are actually international, cross boarder problems; but governments are still running on a national basis and are becoming increasingly nationally focused in the last few years. So whether it's trying to find a globally coordinated response to the pandemic, or a response to the financial problems, or even just cope with the information flashing around the world, there's a real governance issue today. So long winded way of saying no, sadly not. We have connectivity and contagion at unseen -- sorry unimagined levels, but we're still stuck with old fashion styles of government.

00:45:00

James Furman:

I share Gillian's concerns completely that we have international problems and national solutions to them. That's not something new, I mean, financial crisis spread all around the world in a very virulent way in the 1990s. We actually do have some things we didn’t have then. We have a European stability mechanism, an institution we did not have a decade ago, which is part of why countries like Italy are able to borrow now, because there are institutions there that we didn't have before. The IMF does have more resources than it had going into the last crisis. None of that is enough; we need a lot more of that. We need to push a lot further towards economic integration, but the problems were facing aren't new and in some ways we do have some new and expanded institutions that are taking a little bit of the pressure off this time around.

Gillian Tett:

You know, if you go back to the core question, are we better prepared than 2008?

00:46:01

In 2008, you actually had the G20 come together and do something. People like Gordon Brown and others, the former U.K. Finance Minister, actually rallied the G20 countries and they actually laid out a clear cut plan. I mean, where is Gordon Brown when you need him? Basically the G20 has been largely toothless this time around. We have had effective central bank coordination, but in the column of problems it suggests the world is less prepared than in 2008.

The lack of effective global coordination, and the fact that in many ways it's gone into reverse, because the Americans at best lukewarm attitude towards that is another factor which is showing how it's less well prepared.

Jason Furman:

Yeah, I'm certainly not going to defend the G20 or the vigor of their reactions. But if you told me that Italy, a country that's had a terrible economy, that has a huge amount of debt, that has been incredibly hard hit by the virus, could borrow at interest rates of less than 2 percent is, you know, a bit of a testament to the fact that there are some international arrangements, in this case at the level of Europe, that are working.

00:47:15

Because no one is lending to Italy at that amount just because they think Italy itself on its own is good for the money.

Gillian Tett:

But then what you're basically saying is, "hurray, the European Union has not fallen apart yet, or the Euro Zone has not fallen apart yet." I mean, don't necessarily presume it's going to last because you're seeing rising anti-European Union sentiment in Italy. And you're also saying, "hurray, the ESB has flooded the market with so much cheap money that, you know, investors are at least providing some finance to Italy." But that isn't a sign of enormous confidence in the system, and it's certainly not a sign of a financial system that's working in a healthy way.

John Donvan:

I want to go to one more question.

00:48:00

And this one comes from Rick in New York and it actually goes to what we've been talking about. So Rick, welcome to Intelligence Squared. And Rick basically is saying, people are saying this is not a time to be worried about deficits, our government can just print the money it needs. And Rick asks: when did deficits matter? Gillian, why don't you take that first.

Gillian Tett:

Well deficits matter if you can't persuade investors to buy your debt or bully them into doing so. And whether they do or don't depends partly on whether they think that your country is an attractive bet to lend money to, but also what the other alternatives are. And in the case of America right now, it has the advantage of having a reserve currency and the ability to keep printing money. And it also has the advantage that, although things look bad in America, they look pretty rubbish everywhere right now. So it's the question of beauty parade, it's more an ugly parade.

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And you can -- you need to be the tallest man in a room or tallest women in a room sort of, you know, pick me over anything else. The problem going forward though is, will domestic investors keep buying American debt? If you end up in a situation of financial repression, where essentially people try to cut the debt burden by having negative real rates, will you have to force them to keep buying American debt through regulations or constraining their options elsewhere in what's called financial repression? That's exactly what happened post-World War II. I suspect its where were heading in the medium-to-long term. And will other countries keep buying American debt? Will geopolitics break down to a point where maybe they don't want to, or where other alternatives, say and home, in China, or other parts of the world look more attractive. We don't know. But that's the point when the deficit will start to matter.

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So yes, right now people are buying treasuries because there's no one else to buy; it's a pretty grim scenario. But it will be an even bolder bet to presume that lasts forever.

John Donvan:

And Jason, same question to you. Basically comes down to when do deficits matter in this conversation?

Jason Furman:

Yeah, I mean, people keep moving the yardstick and predicting, you know, just around the corner interest rates are going to shoot up and all sorts of problems are going to happen. And that keeps not materializing. I think that, in part, because what Gillian said is if all countries debt is going up, you know, who are you going to turn to? What assets are you going to buy? And ultimately what matters for fiscal sustainability is that you have an economy to repay that debt. And if you don't undertake that debt -- because right now there's a huge liquidity crunch because of a huge economic crisis, and if you're not undertaking borrowing to deal with that liquidity crunch you're not going to have an economy left.

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And that's the biggest problem you could have with fiscal sustainability.

John Donvan:

All right, that concludes round to of our Intelligence Squared U.S. debate, and in our closing round you each get to make a summary statement one more time to try to persuade people who are watching the debate and listening to the debate to vote for your side by going to our website. So round three, closing statements by each debater in turn. And we'll start with you Jason Furman. You have two minutes.

Jason Furman:

Thank you so much. There's all sorts of ways that we were not prepared for this, all sorts of ways that we did not respond well to what's happened. Almost all of those are on the health side, with preparing for a pandemic, with having tests ready, with doing earlier lockdowns, and the like. The part of our system that has functioned well has been central banks around the world.

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The fiscal policy of taxes and spending hasn't been perfect, but it's been quite good. Governments had a set of tools that they knew how to use from the last crisis, and this time they rolled them out much faster than they did last time at a much larger scale than they did last time. And as a result, while we still have a lot of economic damage, and I expect us to, they have been able to keep it contained because it hasn't blown up the financial system also. That will take a lot of things. Gillian pointed to a lot of extraordinary actions that the central bank has taken. You are going to take extraordinary actions in the face of an extraordinary and almost unprecedented economic crisis, and I'm glad that the global financial system was better prepared to deal with this crisis than we were 12 years ago. And I hope you join me in supporting that position on the resolution.

00:53:00

John Donvan:

Thank you Jason Furman, former Chairman of the Council of Economic Advisors, and now to make her closing statement against the resolution, Editor-At-Large at the Financial Times U.S., Gillian Tett.

Gillian Tett:

I would argue that if you want to understand what's happening today, think about that infamous Maginot Line, or the offenses the French built after World War I to try and prevent the German's from invading using what had happened last time around. We have a very similar situation right now. And in some ways it's even worse, because essentially the authorities have already used up a lot of their ammunition seemingly quite needlessly in recent years by keeping interest rates ultra-low, and by letting debt racket up to dramatic levels even in the so-called peace time, even in a boom. At the same time though, they were so busy preparing for the last crisis that they missed some of the problems that were likely to come this time around.

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And by that I mean, not just by not focusing enough on the pandemic, but, say, being so obsessed with mortgage securities that they failed to see what was happening in the corporate and leveraged loan world. So we're now in a situation where essentially the central banks are having to double down to extraordinary degrees, to step in the markets, to essentially meddle in the markets to the point where they are increasingly not necessarily functioning like free markets anymore, and without a clear exit plan in place. We've seen incredible volatility already. It's been dampened down temporarily, but I am seriously concerned about the future because I suspect the kind of crunch we've seen in the last month could end up being simply a foretaste of what is coming. So in many ways, as we've heard in recent weeks, you can't have the medicine be worse than the actual problem it's trying to solve. And I fear that the current wave of medicine shows that the system was not healthy to start with and it's going to be making it sicker in the future again.

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So for that reason, I fear that the financial system was not better prepared for the pandemic than it was in 2008 and I think that's a great tragedy in every sense.

John Donvan:

Thank you Jason and Gillian, and that concludes round three of our Intelligence Squared U.S. debate. The argumentation is over, the arguing is over, and now we are asking you our at-home audience to cast your second vote to tell us where you stand after hearing both side's arguments. You can, one more time, go to iq2us.org/vote. I-Q the number two, U.S. dot org. We'll be collecting votes for, against, or undecided until midnight tonight and then we will announce our winner. And again our winner is based on your votes, the difference between the first and the second vote, whoever's numbers go up the most in percentage point terms will be our winner. So you can again see who won by visiting our website iq2us.org after midnight tonight or by subscribing to our weekly newsletter which comes out every Friday.

00:56:05

So the debate is over; this debate is over, but the financial crisis, the global crisis, the economic crisis, the health crisis certainly is not. And as long as we have the two of you who are experts in the global financial system, surely there are places where you think you agree. We heard some of it and we just want to finish up this part of the conversation with a little more free form conversation. It's not competitive, just to see what you're thinking is going on in the economy. So Gillian, you recently wrote a piece in the Financial Times and the title was "How Much Should It Cost to Contain a Pandemic?" Let's start there. What was the premise of that article?

Gillian Tett:

Well it was basically to try and highlight some very interesting research that's come out in New Zealand where one economists has had dare publish what he thinks is a reasonable amount of spending to make to contain the pandemic relative to the number of potential deaths.

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And you can sit there and question some of the fine details of the calculations; he did that by taking the 1918 pandemic and modeling for the present. So what's interesting is that's a conversation that very few governments have been willing to have in public for understandable reasons, because it's very distasteful and politically contentious as well. But after we come out of this first peak, if you like, and hopefully we are coming out of the first peak, and think about second peaks or returns of the pandemic, it's a question that's going to become increasingly serious. Because unfortunately, the trade-off between massive amounts of spending and economic shocks versus lives saved is something that is not just difficult to make, but it also pits different generations against each other. So I salute the New Zealand economist in question, Bryce Wilkinson, for actually talking about this in public, but I suspect we're going to see more of these kind of papers going forward.

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And I hope we are mature enough to have a proper debate about what the best path is.

John Donvan:

Jason, I was reading an interview you gave back in early March when things were beginning to unravel in the United States and somebody asked you, like, what should the Fed be doing, what should the U.S. government be doing and you basically wrote out a menu of options almost all of which they've now taken up. And you were talking about trillions of dollars even at that time. So in a little bit of a sense you have a crystal ball, I suppose. Or at least you're thinking what the experts are thinking. But if we look longer term at what's happening to the economy right now, and I'm not talking about the financial system now, I'm talking about the economy. Where are you looking to see what the lasting effects of this are going to be? What are you most concerned about? What are you going to be watching to make sure that it's not broke, this part's not broken, or if it is, we have to do something about it?

00:59:00

Jason Furman:

Yeah, and let me just briefly address what Gillian said because I completely agree, by the way. In regulation we all the time put a cost on the value of life and we ask is this cost worth it, is that cost not worth it and you need to do that when you have a limited budget, when you have constraints. I think so far there actually hasn't been a trade-off which is to say steps to help protect lives also will help the economy. China did a more complete shut-down in its first quarter than we have done. They had a bigger hit to their economic growth and I think they're going to have stronger growth in the rest of the year precisely because they shut down their economy to a greater degree. So think there are sometimes where there's no trade-off between saving lives and saving the economy; that's the place we've been. I think we're heading to a place with a trade-off

You know, in terms of your question, John, the thing that is the hardest is to keep the supply-side of the economy together.

01:00:01

John Donvan:

[affirmative]

Jason Furman:

You can make sure people have demand. You can write them checks, you can give them unemployment insurance, you can keep the financial system together by using the Feds and central banks lender of last resort function. But if somebody gets fired from their job it takes a while to be rehired. If they have to be rehired in a different sector because the sector they were fired from, you know, is much smaller than it was then it takes even longer. And so, you know, of the people who have lost their jobs, how many were furloughed and get called back versus how many were fired and have to go find a new job? You know, business, how many are temporarily dormant and spring back versus, you know, go bankrupt and get liquidated? Those are the things that will determine how long and painful the economic slog out of this is.

John Donvan:

It's sort of the same question to you, Gillian.

01:01:00

I mean, what do you see as the long-term impacts of the pandemic? You know, if it stopped today, and we know that it won’t, but where we are so far if we stopped today have long-term impacts already been made? And if it does go on, if we have a slow, slow return to more business as usual or if we have a second wave, what do you see as the long-term impacts? What could be fatally broken, or potentially broken, or need to have to be remade entirely?

Gillian Tett:

Well what this pandemic has shown is that we are all linked in a global chain of humanity and if we ignore the weakest link and it breaks we can all suffer. So I very much hope that this is going to create a world of greater awareness of our connectivity. And I hope that out of this comes a renewed appreciation, a need to think about the more vulnerable in society, to think about trying to build more sustainable growth, to recognizing that science matters you can't just ignore it because it seems politically inconvenient, to recognize that sometimes people have to have short term sacrifice and accept pain to avoid longer term risks and potentially to even get longer term gains.

01:02:28

That's my hope. I fear that what we may be heading for is a world where resources are more constrained, where there will be more bitter fights over how to divide up that pie if it shrinks, where you may get more intergenerational conflict, and where the issue of rising debt and slowing growth is going to make all of those choices much harder. And the other thing is that, as someone who trained originally as an anthropologist before becoming a journalist, people's time horizons have become very shortened.

01:03:05

People's geographical vision, oddly enough, have become very much inward looking. And we're moving towards a world of greater localization in our visions, not globalization. And there's a sense of pervasive insecurity, I suspect, that will not go away any time soon. So countering those physiological aspects is going to be very difficult, and that could definitely weight on the economy and growth as well.

John Donvan:

Jason, to wrap this up I like the framing that Gillian put on this of her hopes and fears; what are your hopes and fears? And give us the fears first so that we can end on a hope.

Jason Furman:

I mean, the worst three fears are that COVID-19 stays with us, which is a possibility; that this is the beginning of more of these diseases emerging, which is a possibility; and that it encourages, you know, bioterrorism, and that's a possibility.

01:04:05

In terms of the hopes, you know, I hope that we figure out a way to handle this on the health side, therapeutic, vaccine and the like. The faster that happens the more we can contain the damage. I hope we come together in a global manner going forward to deal with not just infectious diseases, but so many of the problems we face that really do cross boarders and don't lend themselves to a national solution. And I hope people understand that the government, for whatever frustrations and bumps in the road along the way, played a central role in saving millions of lives and in protecting the economy from something much worse, and believe in its efficacy and importance going forward.

John Donvan:

All right, Jason you gave us a hopeful note.

01:05:00

I want to thank you, I want to thank Gillian, both of you one more time for joining us for our first virtual debate and discussion on the unfolding trends of the global financial system. You both brought what we like which is intelligence, and insight, and civility to this conversation. Thank you so much for that.

This is the launch of our new digital debate series where we will be tackling questions in the coming weeks around the electoral college, around the rise of China as a global leader, gene editing, and a lot more and we're doing it all online. So subscribe to our mailing list at IQ2US to stay up to date with our series. One more time, Gillian and Jason thank you so much for making this possible and for making the time, we really, really appreciate what you did here and the way in which you did it, thank you.

Gillian Tett:

Thank you.

Jason Furman:

Thank you.

John Donvan:

And thank you to our at-home audience for joining us and to everyone who took part. From me John Donvan and Intelligence Squared U.S. goodbye, stay safe, we'll see you next time

[music playing]

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This is a rough transcript. Please excuse any errors.