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Global Financial Meltdown: What Went Wrong, What Is Still Going Wrong and What the Consequences Will Be?

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ABSTRACT *– Current international financial crisis of apparently unprecedented scale (ever since the Great Depression of 1929) could have been spotted from afar and should have been nipped into a bud as early as in 2002! Global political and financial elites are not unable to find the solution to it, they are simply unwilling to identify the problem. The IMF and the BIS once again proved to be useless in their own professional backyard, since it was and still is politically incorrect and financially unremunerative to do so. Crisis has been amplified by sky-rocketing food and oil prices, lax regulation of credit derivatives and cheap-money policy worldwide, but essential culprit of this latest global distress is the greed of the international financial community that spawned fancy asset-backed securitized monsters, which came in too many guises and ultimately got out of hand. Financial mutation brought about jitters of illiquidity across the industry and likely return of depression economics. The paper deals with ill-suited handling of the crisis and probably dire consequences for both the present financial architecture in the economic centres and the future of developing countries at the periphery.*

KEY WORDS: *subprime crisis, speculative bubbles, credit derivatives, SPVs, boom bust cycles, bailout packages, countercyclical expansion, (de)regulation, recession, global financial reforms, developing countries*

"This is not the end. It is not even the beginning of the end. But it is, perhaps, the end of beginning"
-W. Churchill-

"We are both always and everywhere better off not dealing in lemons at all – because what goes around comes around."
-U. Haque-

Introduction

This what we're going through is the fifth global financial crisis in the last three decades,[2] and by far the biggest one after WWII. According to the IMF, immediate and direct losses in the form of balance sheet write-offs amount to 1.45 trillion $ [IMF, 2008] and rising while investment bodies are still being counted throughout the world financial centres. Massive bailout schemes earmarking even greater, breath-taking sums to be injected in the nearly collapsed financial system on a top of dead weight losses, shouldn't surprise us given that the combined equity capital stock of all US financial institutions is roughly $1.2 trillion dollars [Sinn, 2008]. Five global investment banks, nevertheless, succumbed to the crisis already, with Wall Street, City of London, Moscow, Tokyo and Frankfurt stock indices nose-diving for longer than anyone cares to remember. Some countries, notably Iceland and Pakistan, are likely to fall off the cliff without globally coordinated rescue and worldwide recession is by now a clear and present reality [The Financial Times, 2008].

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[2] World debt crisis of 1982, S&L and stock market crisis in late 1980s, Asian crisis of 1997 and particularly global financial crisis of 2001 predated the latest subprime mess.

The tongues, who claim that the worst is over, are the same ones who blatantly (mis)took progressively degenerating flew for a benign autumn cough back in ‘01, ‘07 and ‘08 alike. I'm afraid that the global financial turmoil may have only just begun. “While we have a process, we don't have a definition”, F. Engels often used to say. Yet, bewildering times are instances when scientists cannot afford to be quiet at the expense of being potentially wrong. By now, we all know how the mortgage-backed tsunami first splashed in August 2007 and the fearful word “subprime” crept into the public discourse. Perhaps we don't gather enough on why neither G7 nor IFIs did anything substantial about it? Even more so since the paper boom was out there already in 2001/02 crisis, when banks were let off the hook and allowed to repackage and sell of their “smelly assets” only to inflate the non-banking portion of the speculative balloon and let the global financial bomb ticking [Malovic, 2006]. Moreover, in spite of the fact that dramatic transformation of international financial architecture is both needed and inevitable, it is too soon and even more so dangerous to reinstate Marxian communism in capitalist globalisation. However, the rise of pretty linear state interference and announced backlash of financial regulation among defenders of democracy and liberal capitalism themselves, are not directing crisis management or longer-term reforms in the right course either! Lastly, little is understood as yet on the far-reaching consequences of (handling) the global financial meltdown for the future of international banking and finance as we know it, let alone for the probability of lower-intensity lagged explosions across developing world in financial as well as real economic sense. The rest of the paper is stretched along the timeline of causes (past), management (present) and potential consequences (future), so as to tackle these crucially important issues.

What went wrong?

When growth is high as well as seemingly sustainable and money is cheap[3] and abundant, bankers tend to expand. That is so because low inflation, lots of liquidity and stable economic growth almost invariably produce real estate and other asset price bubbles which have “windfall (capital) gain” written all over them. While expanding aggressively or simply to keep up with their greedy competitors, bankers soon run out of credit-worthy prime borrowers. Hence, they went for subprime ones charging somewhat higher interest rate.[4] In nice weather terms, this initially glided very smoothly. Mortgage loans were government supported business in US, many borrowers got comfy grace periods[5] and hoped for either salary increases (due to unprecedently long period of impressive growth in the US) or cozy refinancing deal (due to capital gains from ever growing real estate bubble). Some of the expectations and suppositions of home buyers were obviously not well founded in foul weather conditions, but still there would be no crisis whatsoever without credit securitization [BBC Business, 2007].[6] It frees banks´capital (often more than once) and enables them to earn more fees by extending loans which are effectively disbursed by other financial intermediaries willing to buy MBSs, CDOs and

[3] Unrestrained credit boom, as first noted by Kindleberger (2000), has always been the main ingredient of the build-up to financial crisis. Following Jubak (2008), current global financial fallout was arguably amplified by many additional circumstances that made the money cheap and credit abundant: 1) stubbornly expansionary interest rate policy of FED to fend off economic slowdowns during dot com and in particular after the NASDAQ bubble, 2) a weak yen and almost zero real rates in Japan which enabled speculators to engage in carry trade or massive security purchases elsewhere, 3) a gigantic surge of exports from emerging giants determined to hold down their national currencies and domestic absorption, and not least due to 4) soaring petro-dollar profits which were reinvested in Western banks just like three decades ago.

[4] As a rule, the spread charged is circa 2%. Subprime borrowers, aka „B“ or „second chance“ borrowers, are individuals with FICO credit score bellow 620 (on a scale from 380 to 850), who are taking loans considered risky both for lenders and themselves [NematNejad, 2007]. FICO score is credit-analysis synthetic which shows how likely one is to repay the loan, pending –among other things- on monthly earnings, credit history and amount of accumulated debt still unpaid. Alternatively, subprime borrower is the one who doesn't qualify for Freddie- or Fannie-supported mortgage.

[5] For example, usually offered deals included: interest only mortgages, or adjustable rate mortgages, or even low initial fixed rates [Gorton, 2008]. Some brokers went as far as supplying “no doc” mortgages which do not require any evidence of income or savings [NematNejad, 2007].

[6] Credit securitisation implies pooling together several active (still unpaid, immature) banking assets and offering them as collateral for third party investment in yet another derivative asset.

alike credit derivatives issued by investment banks.[7] The catch being that many financial institutions are prohibited or at least restricted by law from buying subprime debt or risky credit derivatives.

In order to circumvent the regulations, just as so many times before, investment bankers came up with novelty – they chopped off the subprime portfolio into half a dozen of tranches, defining the pecking order of risk taking if and when any of the subprime borrowers from the pool defaulted. As the notes from different tranches, senior (AAA), mezzanine (BBB), subordinated (A) and equity note (junk), carry different ratings, there is so-called cash flow waterfall, i.e. priority of payment, which attracted otherwise skittish or legally-constrained investors too. Problem with CDOs as opposed to CDSs and other balance sheet derivatives lies in the fact that the asset pool in contemporary CDO typically is not static, in other words it is being actively managed for better or worse [Anson *et alia*, 2004]. Credit enhancements[8] and rather questionable (up)grading methodology of credit rating agencies[9] blurred the investment picture a step further. However technically suffocating as it may seem, such a malevolent usage of credit derivatives is not horribly innovative, nor illegal for that matter. Confronted with bad loans and foreclosures coming from media sector and window dressing performed by discredited auditing agencies back in 2001/02, international banks did exactly the same trick and got away with it.[10] Once again, genetically mutating credit derivatives enabled investment banks to get rid of the large portion of the subprime loans as debt instruments with above prime credit ratings thus expanding the number of potential buyers of that debt and, in fact, making money on it!

Nevertheless, by offering better returns on the riskier slices of portfolio in order to attract suckers to buy them, banks had to lower the yields on the super senior tranches (since the overall cash flows from the pool backing a CDO is given). That made it harder to sell senior slices once they became “a liability” and practically forced many banks to keep them on their own books after all [The Economist, Dec.8th-14th, 2007]. On the other hand, recent surge in exploiting synthetic CDOs made risks global banks were exposed to even more obscure. Obliged by the law, intermediaries that held huge amounts of these instruments kept them in semi separate off-balance sheet entities, legal shells called SPVs, so as to allow themselves more business flexibility in accounting and regulatory terms. SPVs fund their operations by frequent roll-overs of short run debt which is then used to buy longer run debt. Now, synthetic CDOs[11] enable removal of credit exposure without actual asset transfer (and costly administrative burden of true sale of the underlying) to SPV. In addition, through intense use of credit derivatives, synthetic CDOs transfer credit risk directly from the sponsor (originator of the transaction) to the end buyers, so that after delinking, investors have no credit exposure to the sponsor. A synthetic arrangement also means that the risk of assets otherwise not suited for securitisation (bank guarantees, letters of credit etc.) may be transferred [Anson *et alia*, 2004]. Nonetheless, assets in question stay on the banks´ balance sheets! And indeed, contradicting one of the fundamental aims of securitisation, it doesn’t seem that this time, “thanks to” synthetic deals, the awful lot of credit risk did leave the banking sector via financial innovations, but was rather shuffled around instead! When unmonitored credit boom, adverse selection and increasingly worsening financial visibility brought about first losses and suddenly slipped into a slump, interest rate differentials turned against SPVs and the hell broke loose.

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[7] These other financial intermediaries were also banks, but often much more vulnerable investors like insurance companies, pension funds etc [NematNejad, 2007].

[8] Overcollateralisation (meaning that overlying notes are engineered to appear lower in value compared to the underlying portfolio), cash reserve accounts (liquid contingency account to cover initial wave of losses), excess spreads (which deleverage derivative) and insurance wraps being the most frequent form of enhancement [*Ibidem*].

[9] Which are competing with each other and which in any case, it has been proven, cannot accurately calculate credit rating of structured products which contain market material by many issuers [Malovic, 2006].

[10] Citigroup and J.P. Morgan Chase, the biggest creditors of Enron and WorldCom (companies whose default put together represent greatest corporate loss of all times-34 bill.$), in the second quarter of 2003 already announce billions in profits! Deutsche Bank reduced its loan assets for 40% in 2002 and early 2003, ABN Amro transferred 34bill.$ of credit risk and Credit Suisse and UBS “freed up” more than 10bill.CHF each [*Ibidem*].

[11] Synthetic CDO consists of two legs: a short position in CDS (bought protection), by which the sponsor transfers portfolio risk to the issuer and a long position in a portfolio itself (of bonds and loans), the cash flow from which pays liabilities of overlying notes [Anson *et alia*, 2004].

What is still going wrong?

Just about everything! The problem being, nobody truly knows what this collapse is all about. And yet, national authorities were mostly prophesying about how the end is near. In such a cocktail, panic and recession are regrettable, but not surprising by-products. In a nutshell, instead of recognizing it, we are still throwing money at the problem.[12] Libertarians in office around the globe have been advocating elaborate plans to do little more than nothing. Neo-socialists on both sides of the pond are still screaming for "dirigisme" and ritual purging of every institutional pillar of free market capitalism. As an arithmetic mean of those voices, we have lots of newly released liquidity flashing around[13] and not much hard thinking: amazing rescue package of nearly 1 trillion US$ apparently left investors more or less unimpressed. Heavy government spending earmarked for 2009-10 is on its way as an attempt to mitigate bone-freezing recession in the US and consequently worldwide. In fact, European and US policymakers are doing exactly the opposite of what any money and banking textbook would suggest. They proved to be genuinely lenient towards moral hazard of the financial sector, they are bailing out and even recapitalizing greed- or competition-driven banks by taxpayers' money, they are mistreating the meltdown as liquidity crisis, whereas the confidence game at hand has much more to do with systemic failure, they are making unsecured loans directly to corporate sector etc. Moreover, too slowly disappearing information asymmetry within the overregulated banking sector is being accompanied by asymmetric information in policy arena as well as real economy, while suggestions for reforming the (inter)national financial architecture, rectifying bad off-balance policies and strengthening global financial oversight are frankly varying from ignorant to scary.

Some are blaming the <u>subprime market</u> for financial Armageddon, yet they are only shooting the messenger.[14] Others, German finance minister as the most prominent among them, are accusing <u>the US</u> in as much as Americans exported their toxic assets, bad (de)regulation standards and cut out their import potential.[15] Yet some are accusing <u>the IMF and the BIS</u>, while forgetting the fact that developed countries themselves, for the past decade or so, deliberately avoided and dwarfed those IFIs both in terms of financial and policy making relevance [The Guardian, 2008].[16] Another lot is blaming <u>the illiquidity</u>

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[12] Stiglitz (2008) rightfully compares the ongoing bailout to massive blood transfusion to a patient with severe internal hemorhaging. Congressional revisions, in my opinion, only increased the sum but regretedly decreased the effectiveness of the rescue package.

[13] Even that being possible without instantanious inflation cost only because or exactly because the eventual fall of crude oil price in the world markets.

[14] Indeed subprime market was the fastest growing particle of real estate market: 21% of mortgage applications between 2004 and 2006 were subprime compared to 9% between 1996-04. Subprime mortgages reached a record of $805 billion in 2005. However, statistics show that only 3.3% of subprime loans end up in foreclosure compared to 1.1% for conventional loans [NematNejad, 2007]. Without the help of greedy bankers and exuberant independent brokers who originated the dodgy underwritings, this number would hardly provoke an international crisis. Mortgage market is one of the most regulated segments of US financial system, and even though almost 12 million mortgages were contaminated as the real-estate bubble started to deflate [Stiglitz, 2008], only some 2 million foreclosures actually took place so far.

[15] This is downright stupid since US BoP position represents nothing more than a mirror-image of someone else's willingness (not obligation) to invest in its financial system, whereas not even economic superpower can be deprived of adjusting its import demand elasticity in the face of balance of payments/currency adversity. When it comes to financial regulation, Europeans (unlike the US) implemented Basel 2, which obviously didn't do miracles for prudential supervision either. Nonetheless, the first circumstantial causes of the crisis do lie with Clinton's repeal of the Glass-Steagal Act [Chossudovsky, 2008] and the Fed's monetary ease, i.e. responsibility for it rests with the US. "If too much money was lent and borrowed, it was because Chinese savings made capital cheap and the Fed was not aggressive enough in hiking interest rates to counteract that. Moreover, the Fed's track record of cutting interest rates to clear up previous bubbles had created a seductive one-way bet. Financial engineers built huge mountains of debt partly because they expected to profit in good times - and then be rescued by the Fed when they got into trouble" [Mallaby, 2008, p.1]. However, after becoming aware of the possible demise of Northern Rock in the UK and several Landesbanken in Germany, Europeans did exactly the same thing. According to Trichet (2008), since August 2007 ECB injected almost 300 billion € to stabilize euro-area money markets.

[16] Having said that, the IMF and BIS did fail us big time, however, not so much due to the lack of human and financial resources, but for lack of courrage and professional ethics to say the truth. Priminister Brown's and Kanzlerin Merkel's recent statements bear the taste of tautology at best or cynicism otherwise, when they urge for reform of the global financial system which will empower IMF and BIS with maintaining international financial stability and capacity to act as an early warning system for markets!

paradigm for financial cardiac arrest.[17] In fact, and for deep theoretical reasons, the world financial system has collapsed into insolvency, but before prescribing the diet and exercise, we had to restart the heart. "Nuclear option" might eventually work beyond and above the fire-fighting call of duty if re-capitalized financial system picks up and returns to the precrisis lending pattern, but only provided that the asset price bubble subsequently gets back at least some of the air it lost through deflation process. Nonetheless, even if it doesn't, there's a widespread consensus among both academic economists and practitioners that political, financial as well as business cycle consequences of standing idly by for taxpayers across the globe would be even dearer. On the other hand, nobody likes recessions, nor over-turning tables, hence, devil's advocate could argue that taxpayers raw deal could have been stricken more wisely if spent on unemployment benefits and SME tax holidays for investment in real capital, rather than on bailing out reckless speculation [Shiller, 2008], [Stiglitz, 2008]. Lack of regulation argument is the last but the most frequent and more misleading among the usual suspects. Yes, we certainly long for "reconstruction of creative destruction" epitomized by originate-and-distribute structured products, having in mind that -dipped into globally wandering liquidity- they created a favourable breeding ground for quite shockingly imprudent risk taking [McCreevy, 2008]. However, my argument is that too much regulation in banking sector has been equally disastrous as too little regulation in the rapidly expanding non-banking industry! On balance, we need as much further deregulation in the banking sector as additional regulation in banks' off-balance sheet activities and overall activity of the non-bank intermediaries.[18]

What the consequences will be?

It would be impossible to foresee every single crossroads where international financial crisis management might go awry. Thus, this last section may in fact push more on the normative side of the argument: what should the corollaries be, and therefore, what additional consequences might be lurking downstream.

Whatever happens, the world is unconditionally heading towards murky waters of re-regulation, significantly more government involvement in economic activity and strikingly larger budget deficits. With counter-depression Keynesianism back in macroeconomic fashion, Kyoto-inspired environmental protection is, alas, designated to be probably the first virtuous casualty [The Economist, Oct.11th-17th, 2008].

Big emerging markets like China, India or Brazil, will slow down for sure, but still are expected to grow at 4-5% *p.a.* which takes them out of immediate scope of this paper.

With regard to international financial centres and developed world, the length and severity of inevitable recession shall be chiefly determined by three interdependent developments. First is the ability (and speed) of nuclear option and bank-nationalization cum re-regulation experiment to deliver sustained breeze of reflating asset value into the global financial sales, *caeteris paribus*. [19]Second is the quality of urgently needed reform of IFIs (often dubbed Bretton Woods 2[20]). Third is pending on fre-

[17] In such a constellation, bailout is justified and meaningfully required only during the intermezzo of confidence restitution in inter-bank money markets, whose nervousness is depicted by spread between the LIBOR and OIS or 3 month LIBOR compared to 3 month treasury bonds rate [Taylor-Williams, 2008]. Sadly enough, it has become evident that we are dealing with much a nastier situation here, namely, inter-bank illiquidity reflects the size of announced and estimated losses in the financial system as a (w)hole, i.e. mistrust of non-banking sector in its' own and counterparty's credit worthiness. FED's recent decision to ban "shorting" is only a wrap up on the reasons why hedge funds and the like won't be able to ride in rescue of prime brokers any time soon.

[18] For opposite argument engulfed in much more cynical political connotations see interesting article by Chossudovsky (2008).

[19] Desai (2008) warns that reestablishing credibility of financial system can be just as cumbersome as reestablishing solvency. The Economist (2008, Nov.1th-7th) illustrates the point with first indications of rescue packages being diverted from intended demand-driven use into precautionary household savings and excess banking reserves, without significant impact on the reference rates.

[20] The announced multilateral summit on November 15th could at best draw a blueprint of reform allies for present global financial architecture, something like a wish list of primarily Eurpeans and Chinese in terms of decision-making weight

quency and whereabouts of sporadic financial failures yet to occur among non-banking financial intermediaries. If I was to give condense answer to each of the presently unknown developments it would be: *I don't know*, *I sincerely doubt it* at least in the short run, and *Yes most likely*.

Thus, further reforms on several economic fronts may be safely identified at the horizon, some of them approaching dead ahead, others still spinning in intellectual and/or regulatory conundrum. When it comes to valuation failures, Sinn (2008) swiftly proposed the most resilient version of amending the mark-to-market accounting: company's assets should be valued according to the lower (of historical and current) value principle at tranquil times already, so that bubbles get deflated on the runaway rather than kept artificially overvalued in the midst of crisis.[21] Equally crucial, weaknesses in underwriting and upgrading procedures need urgent attention of BIS or alike global regulator, which has to find the way of attaching the collateralized responsibility for the risk assessment on distribution of asset-backed securities [Wellink, 2008].[22] In a overall perspective, arguably, central banks' operating frameworks for controlling broader liquidity concepts would also have to be improved. As pointed out earlier, a considerable source of funding stems from non-bank intermediaries and is fair to admit that central banks' control over such liquidity is quite indirect and pretty limited [Clerc, 2008], for no profound theoretical reason. The last point of concern is of utmost importance since, in historical retrospect, government purchases of bad assets in the banking sector itself and *de facto* centralized asset-management units usually failed to inforce institutional learning in the core lending practices of lemon banking industry [Desai, 2008].

Depending on their own traits, financial systems can serve as a shock absorber or if the right failure-screws are loosened, may innovate themselves into nasty amplifiers of havoc [Allen-Carletti, 2008]. For some people from financial industry, regrettably, competitive advantage boils down to making markets work less efficiently. One catastrophically diligent way of doing that is to surf on a deliberately raised asset-price tide whose ephemeral nature tends to be secluded by hidden or obscured information [Haque, 2008]. But what about all of us caught off-guard in the shallow waters?

In other word, let me finally turn to the foreseeable consequences of global financial turmoil for small open developing economies with still emerging financial markets. The good news is that sturdiness of their banking sector presently seems more or less genuine, with separate banking accounts from the parent HQs and no immediate exposure to contaminated loans. Also, foreign exchange reserves of developing countries appear to be bigger and more robust than ever before. On the other hand, even absent the global financial crisis, their precarious macroeconomic position would undoubtedly require them to follow the straight and narrow due to astonishing BoP deficits and steeply rising foreign debts they have amassed. Global credit crunch shall only add up to that. Stock market slump in transition countries we owe to the fact that over there, or in South-East Europe at least, domestic residents represent a minor percentage of securities holders, and majority of, in fact foreign, investors simply flew to safety or fled emerging markets in order to cover losses incurred elsewhere on first signs of global distress. As the sovereign credit-rating scores storm the fire stairs, many of the developing countries overvalued currencies will be finally battered by either contagious, speculative or debt servicing capital outflows, which will supplement - here and there already contemplated- wage freeze and revive

and policy dogmas (e.g. Jayaraman (2008) accentuates notorious Washington consensus and hypocrete double standards in stabilisation requirements for South vs. North) which should be fundamentally altered, but not much would happen hastely and without consent of the US, who's new administration is still in the forming and simply isn't ready for anything of a Bretton Woods 2 scale.

[21] "It is difficult to keep a proper perspective and to exercise prudent judgment when all of your competitors are generating huge volumes of business. As one banker famously said last year: *As long as the music is playing, you've got to get up and dance*. Well, if it is the role of the central banker to take away the punch bowl just as the party gets going, perhaps the role of the supervisor is to silence the band so the bankers stop dancing." [Wellink, 2008, p.2]

[22] Rating agencies consider themselves answerable for assessing credit risk solely, whereas investors typically reckon with liquidity risk being accounted for in leading agencies' ratings too. Moreover, the metric used for structured product rating is identical to methodology used for simple bonds [Clerc, 2008]. In addition, if unresolved, this aggravates the awkward marriage of chiefly national bailouts and evidently international contagion [The Economist, Oct.18th-24th].

competitiveness in the medium run.[23] Meanwhile, exporters will have exhaustingly hard time to keep - let alone acquire new- foreign market shares, hence macroeconomic reply through pseudo-governmental export promoting banks and agencies should prop them up in their utmost capacity.[24] Crisis-provoked savings hike will prove detrimental in the shortest run, which is why the attempt should be made to replace the absorption loss by public infrastructural project spending and officially negotiated bilateral investment-related debt or equity inflows. Unfortunately, FDI, cross-border credits and other forms of international capital expansion are certainly going to shrink too, now when wealthy countries' businesses are suffering from recession themselves.[25] Similar drying up of remittances could be reasonably foreseen together with vanishing of multilateral and official transfers. In spite of alarming external position, monetary policy stance in developing countries needs to remain roughly neutral, with FX reserves used up for running the foreign debt down rather then for dissipation in defense of the misaligned national currencies. Obsolete austerity orthodoxies of the IMF should be kept at minimum until its deregulate, liberalize and privatize ideology is reduced so as to deliver faster and more obvious net-benefits for IMF's protégés. For those aspiring a soon EU accession as a last resort, sufficient is but the gaze at the institutional, financial and political tears in the fabric of the European project cruelly exposed during the international financial meltdown. The odds are that there shall be no swift enlargement, and if it happens after all, newcomers might be developed countries (like Iceland and Norway) rather than any of Balkan states. Provided that non-EU developing countries came to terms with their infrastructural, public administration and corruption insufficiencies, their end of recession tunnel may be in attracting the already deployed neighbouring businesses looking for cost-cutting asylums.

One way or the other, developed countries shall recycle and spread the burden of the crisis onto the rest of the world. Asian economies learnt the lesson of their own financial gambling and felt the bitterness of double-edged IMF policies only too well back in 1997/98 [Hüfner, 2008]. And indeed, by and large Asians appear not to have stepped on the wrong parts of financial minefield so far. If this *ad hoc* reasoning hints at any conclusion, I am at the point of suggesting that the next international crisis might touch upon the still unthrusted bubble economies, namely South-East Europe or even Russia itself.

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[23] The conventional caveat reminding that exchange rate changes coupled with popping of real estate bubble can result in large losses in the banking system and eruption of full-blown crisis if the banks passed on too much loans with foreign exchange clause onto debtors that lack foreign-currency revenue [Roubini-Spetser, 2004].

[24] However, for the time being, export-credit finance and infrastructure projects with spill-over effects remain the only two elements of fiscal expansion I would advise for.

[25] Outgoing structure of FDI in South-East Europe reveils that almost a third of the money ended up in real estate, feeding the local asset bubbles still standing only because of uneven demographic distribution biased towards the urban centres.

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