

Book Review

FAULT LINES

HOW HIDDEN FRACTURES STILL THREATEN THE WORLD ECONOMY

**Raghuram G. Rajan, Harper Collins Publishers India Ltd., 2010,
ISBN: 9788172239732, pp.288(HB), Rs.499/-**

Fault Lines won the Financial Times and Goldman Sachs Business Book of the Year Award 2010. Raghuram Rajan saw off strong competition to win the £30,000 prize.

The financial collapse of 2007 and the recession that has followed left the world awestruck. Rajan has been one of the few economists who could sense the global financial crisis approaching. His book gives an explanation of what went wrong and gives a framework to avoid such recurrence. The book identifies the flaws that crippled the world financial system and believes that it is not just the few greedy banks and the bankers who are to be blamed but the serious flaws in the economy are also to be blamed. There has been growing inequality in United States, which combined with a weak safety net, created political pressure to encourage easy credit and keep job creation sturdy. With low purchasing power of middle-class household, there was an urgent need for credit. The financial sector, with encouragement of the government, supplied home-equity loans, sub-prime mortgages, and auto loans at easy rates. The after effects of it turned out to be really devastating.

He highlights the concern at three levels. His first concern lies in United States, because of a thin and feeble safety net, the government responds to global downturns with too much stimulus so as to avoid job losses. There have been recoveries with regard to job earlier but the problem is that they are responded with the same failed policies again and again. This sets the stage for subsequent financial excess. His second concern being at the global level, the strategy of export-led growth in a number of recent fast-growing countries, including Germany, Japan, and China, has made the world too dependent on a few countries like the United States to be the “demanders of first resort”. Lastly the concern is for the US financial sector, which is the critical but unstable link between an over stimulating America and underconsuming rest of world.

Reforms suggested in the book, at the global level, are that countries need to become less addicted to exports, so that they can pull along with the United States in getting the global economy out of the periodic ruts it gets into. United States needs to create a better safety net and has to also put focus on improving access to quality education, as it is the inequality in education that sets the stage for a lifetime of continued inequality. Lastly, he believes that the financial sector needs huge reform. The reform though, should not be a simple response as to increase capital requirements for sub-prime mortgage backed securities for it will only push the excess somewhere else next time.

The epilogue of the book summarizes the whole story:

“The crisis has resulted from confusion about the appropriate roles of the government and the market. We need to find the right balance again, and I am hopeful we will.”

Shipra Singh

The book clearly suggests if proper care is not taken and the root causes are not addressed soon, more severe crises could arise in future, and the book would certainly question some long-held biases about current state of economic conditions in Western countries.

The book has ten chapters with an introduction in the beginning and an epilogue at the end. There is a special chapter on India – “Afterword: What Lies Ahead for India”. Rajan believes that if India with its many communities, languages, religions, and castes can pull it off, it would be an inspiration to many poor countries.

The steady decline of India’s once superb universities need to be reversed, and create such universities that would recruit the best faculty from around the world to teach India’s youth, nurturing the kind of research and thinking that will help create a modern, a unique India, that would have different opinion towards economies, culture, politics, society, and international relations.

“The world has much to gain from a successful India.”

The book is a must read as it paints a clear picture of the economic forces shaping the world.

– *Shipra Singh*