



Interview with Xavier Sala i Martín

«Regulators are no good to prevent crises»

NÚRIA PELÁEZ

The crisis we are just leaving behind has not been the first, nor will it be the last. According to [Xavier Sala i Martín](#), a full professor of Economics at [Columbia University](#), it has been just «another one», and learning from the errors that brought it about will not avoid further ones. What really concerns Sala i Martín is that the psychosis created by this crisis has wakened up two of the most fearful monsters to economic liberals as he is: excessive regulation and trade protectionism, two problems he believes they can cause a disaster out of an ordinary crisis. But the economist who made colourful blazers popular on the ranks of the Camp Nou stadium is optimistic: «Capitalism is wise and the market will put everything in its place.» However, he is more critical in setting out a competitiveness strategy for Catalonia and Spain, for which he recommends to go for applied innovation in all industries. His advice for politicians is: «Just copy FC Barcelona.»





Do you think that a far-reaching and deep crisis as the current one is just a cyclical phenomenon, or is it catalysing new trends and realities, so we will get out of the crisis in quite a different situation from the one that led us to it?

Crisis is inherent to market economy, there have always been and there will always be. This is just another crisis, and not even the biggest. Quantitatively, for instance, it has nothing to do with the Great Depression, which had a much larger impact. However, we can also learn from crises, as we do from plane crashes, though the next crises will probably have different causes. What can happen is that a different system comes out of it. The regulatory system has been blamed for it and a more interventionist than the one we had before will eventually be created, and this will be bad. A great fallacy is being created. Spain, for instance, has already too much regulation, and if we allow regulators to rule the world again things will get worse. This is especially true for the Third World, where governments traditionally have tried to meddle in the economy, which has placed a too large burden on their countries. And now they were starting to get out of it they will fall back as the lack of regulation has been considered to be responsible for the crisis. The problem of believing that the solution is more regulation lies in that regulators don't know what they do. The banks in the US and in many other countries have given credits to people unable to pay them back and the Basle rules allowed them to take mortgages, package and sell them to subsidiaries. A regulation was clearly in place.

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The problem is that it was done the wrong way. Now they will change these rules and think that this will solve it all. But they are wrong because the next crisis will come from a different side. The problem of believing that everything will get all right with regulation is that excessive regulation can halt progress, and we don't want that to happen.

Regulators are not as fast as innovators. In the case of Spain, Prime Minister **Rodríguez Zapatero** wanted to teach lessons on regulating the Spanish financial system at the **G-20** Washington summit in November 2008. Curiously, they didn't see the problem with real estate. If the Bank of Spain had such a great foresight to anticipate that American toxic assets would cause trouble, why didn't they prevent the banks from concentrating so many loans on the building industry, which was after all the cause of the crisis in Spain? Regulators are clearly no good to prevent crises and the belief that they will avoid future ones is false and will lead us to failure.

Many countries from the US to Catalonia and Spain have turned capital to speculative activities with short-term profit to the detriment of productive activities with a long-term view. Do you think that incentives having allowed that will change enough in order to avoid a crisis similar to the current one to happen again in a few years?



Human beings are out for quick money. When there is an activity that yields profits above the average, everybody goes for it and it creates what we economists call «bubbles». If bricks and mortar become suddenly fashionable, prices rise, people buy, prices still rise, and so on. This is a natural trend in humans, and others will come up. What has happened now is what occurred in the 1990s with the dotcoms, which were considered a safe investment. But all this has nothing to do with the nature of the system but it is related to human nature.

How do you think the insufficient tendency to saving in the United States and Western economies and excessive dependence on foreign financing by countries such as China can be reoriented?

I think this will be corrected on its own. One reason for which Americans were not saving was because they had the mentality of easy money, but this is already changing. Precisely one of the problems the US have today is that people have stopped consuming and save as banks don't lend money and prices have gone down to former levels. What is a problem is that the Chinese have kept

their currency artificially low and thus the US dollar artificially high. The Chinese strategy of unlimited export is an imbalance that will also be corrected alone as the way China keeps its currency cheap is buying dollars and selling yuans. They are creating a huge inflation, so prices in yuans will rise a lot with time and this strategy will die out. The day will come when a Chinese won't know what to do with so many dollars and they themselves will see that this makes no sense, that they are the world factory in exchange for sheets of paper with George Washington's face printed on them. They will need to use this money one day and then they will get prices down. The economic system has its own correction mechanisms.

There are people who believe that the crisis at General Motors was unavoidable and has just accelerated with the overall crisis. Are industrialised countries doomed to lose most of their traditional industries, or are there alternative models making them feasible?

There are big car manufacturers doing very well in the United States: Toyota, Nissan, Honda... The reason for which General Motors and the other Detroit companies had problems is that in order to prevent the 1980s general strikes from happening again, they granted trade unionists a lot of things they were asking for including expensive pension schemes they are paying right now. It's not a problem of productivity or technology because in the state next to where General Motors is based there are Toyota factories that are doing very well. So the problem is not a lack of productivity of the American industry. It's obvious that the US are able to make cars, otherwise Toyota wouldn't be there manufacturing them. What is more, if we think well, the future of cars at a global level is bright. Only think that Chinese incomes are just starting to rise and cars will be needed for over a billion people, and the same will happen in India. Besides, green cars will come up, which will mean a renewal of the current car pool. So demand for cars will be high in the coming decades and so will multi-billion benefits for those able to do things well. We have missed the train to make products that are manufactured with low wages, but we can make them

The economist with coloured blazers

Arranging an interview with the economist Xavier Sala i Martín (Cabrera de Mar, 1963) means to fight against the busy agenda of a man living between New York, where he is a full professor at Columbia University, and Barcelona, where he teaches at the Pompeu Fabra University as a visiting professor and is the head of the economic area of the FC Barcelona. Sala i Martín finally meets Paradigmes in a Barcelona restaurant on a Friday afternoon, sparing more than two hours of his valuable time for us. He tells us that he usually goes there for lunch after playing football with friends – though that day he was unable to do so – which shows that his admitted passion for this sport is not restricted to enjoying it from the ranks of the Camp Nou stadium. Sala i Martín honours his long teaching career, talking in a didactic and straightforward way, completing his explanations with all kinds of examples and comparisons, defying the risk of oversimplifying. Used to his peculiar colourful dressing style – especially as to his choice of blazers – it is surprising to find him fully dressed in black, with a watch around each wrist, perhaps because living on both sides of the Atlantic causes considerable time hassle. However, once he sees the photographer, the economist quickly dresses a garish red blazer: the object lens awakes his most glamorous image.

Xavier Sala i Martín graduated in Economics from the University of Barcelona in 1985, and five years later he completed his PhD at Harvard University. He taught later there and at Yale, and since 1995 he is a full professor at Columbia University. He has also been an advisor to the International Monetary Fund and the World Bank as well as a researcher at different institutions such as the Washington Institute for Political Research and the European Policies Research Centre in London. One of the world's most quoted economists according to the Essential Science Indicators, he collaborates regularly with different media. Since 2009, Sala i Martín is a member of the FC Barcelona managing board, having been the president of the club's economic commission since 2004.

His passion for football becomes apparent during the interview as he constantly takes chief coach Josep Guardiola and his players as an example. He definitely has no problems in mixing his academic and football sides. In fact, on his public profile on the Columbia University website, the first visible thing is a large picture on which the professor proudly shows the Champions League trophy won last season by FC Barcelona.

with high added value. There are things in the car industry that require big innovation, investment in technology and skilled workforce, and others that do not. What usually happens is that new products are invented in rich countries

before being passed on to poor ones: this is what economists call «product cycle». Trying to prevent products with low added value from leaving is a mistake, giving subsidies to do so is not the best solution as they will move to less developed countries sooner or later.

Expansive measures taken in China include a commitment to social protection. In the US there is a discussion on universal health care. Are we starting moving towards more homogeneous welfare schemes in industrialised countries and to competition less based on social and perhaps also environmental costs?

It's not clear that health care in the US ends up as in Europe. A serious health debate is not whether the poor shall have access to health care. Of course they should. But this is not what's being discussed. What's being discussed is who takes the decision of going to a certain kind of physician or to another, of using a cheaper or more expensive medical technology, and I think the decision should be up to the patient. As to the Chinese, they will do like the other countries as they become wealthier: they will devote a given amount of money to health care. It's possible that the US move to a certain degree of socialisation, though I don't believe it as people want to decide by themselves there. Another issue is environmental protection. We have gone for the climate change hype and force Third World countries to clean what we polluted earlier. The Chinese are ready to reduce pollution for each GDP unit a bit but are unwilling to sacrifice their growth to make up for the mess in the First World. I think there is no way of negotiating here: they will cut emissions per GDP unit and Americans will accept a minimal reduction, while some Europeans will continue with their self-flagellation and Spaniards will stay in the first row in the demonstration, though they will reduce nothing once it comes down to hard facts.



Will the middle class in industrialised countries be weaker and social polarisation become stronger after the crisis?

No. Right now, those having lost most with the crisis are the rich, those owning real estate and

shares. Obviously, those whose unemployment benefit has run out and still haven't found a job will lose even more if the economy doesn't recover, but generally speaking, the middle class hasn't lost much of its purchasing power. However, countries like Spain will need to think well of how to solve the big problem that is migration. Spain has never experienced a situation as the present one before: there has been migration but things were going well, but if the issue is not solved there will be social conflict. A problem will be created as many unemployed migrants have no family helping them. And if there are migrants working and unemployed Spaniards, there will also be discrepancy. If this social problem isn't tackled, far-right parties can come up and use this issue as it occurred in other countries. And I don't believe migrants leave because of the crisis as to them it would mean to go back to a worse life than the one they are leading here.

«Human beings are out for quick money. After the bricks and mortar bubble others will follow as it is a natural trend in humans.»

Will the United States stop being the driver of global consumption, and if so, what effects will this have?

They won't stop being it as they will remain the wealthiest country in the world. Consumption in the US used to be 25% of global GDP and despite having gone slightly down, it will remain very high. As China and India grow, the significance of the US will reduce as world GDP increases. Since World War II, the significance of the US has been constantly lowering but it is still high. China, for instance, is still a very poor country. Its GDP per capita is US\$5,000, whereas that of the US is US\$35,000. Perhaps they will converge within fifty years from now.

Is the current drop in international trade cyclical or are we seeing a certain deglobalisation? Are we heading towards protectionist

deglobalisation, perhaps based on environmental requirements?

The drop in international trade is cyclical and dangerous as there are protectionist temptations. Rich countries have always looked for excuses so poor countries can't sell. And now the pretext is environment, like it used to be worker exploitation, health conditions, etc. The thing is that they sell cheaper, and as we can't fight them economically we do so politically. This is protectionism. Barack Obama recently set a 35% tariff on Chinese tyres and the Chinese retaliated with a tariff on American chicken. This situation is very dangerous because the big difference between the present crisis and that of 1929 is protectionism. What turned the 1929 crisis into a disaster was protectionism. At the G-20 meeting, after the Lehman Brothers bankruptcy, the first sentence the governments said was «we're not going to do protectionism», but they all have done.



In how far do you think that so-called green shots of the American economy are solid? Do you think there is a risk of being in a W-shaped crisis? What should be done to prevent this?

I think we're in a double-W-shaped crisis, like Bart Simpson's hair. When historians talk of this period one day, they will say that leaders were schizophrenic because the solution they gave to counteract imbalance was creating an even bigger one: demand for more megalomans for governments, which has created a big tax imbalance. At the G-20 meeting they said they were perfectly aware of this big tax imbalance, but they also believed that it was not the moment of doing anything because cutting debt would mean to reduce expenditure and increase costs, which would mean a relapse. This is joined by other imbalances. The first is monetary: to solve the crisis, governments have printed money and the monetary mass has exploded. The most normal to occur is inflation: if it didn't come it's because money hasn't circulated. When the economy recovers, all this money will circulate and create inflation, and when the government tries to stop it interest rates will rise and we'll fall back into recession. Another imbalance is foreign debt, which will need to be corrected. It won't be difficult for the



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FC Barcelona as an example

Xavier Sala i Martín supports the idea that in order to make Spain an innovating country, the first step is to set the foundations of an educational system that helps develop a working and entrepreneurial mindset. «The problem in Spain is that everybody here wants to go to Big Brother and become rich and famous within four months, and this is very harmful», he complains. «Making money requires work.» Sala i Martín likes to come back to his great football passion to give economic examples, and this is no exception. «FC Barcelona players are good because they work. Why is Iniesta so good? Because he has been working for hours and hours ever since he was a little boy. Americans have a mindset of working and effort like the Chinese and the Japanese, though the latter are not so creative; but in Spain this is still difficult.»

US as its domestic driver, Silicon Valley, hasn't stop working, but Spain will have many troubles. A third imbalance is the sectorial one: in Spain, 19% of economic activity came from building and it can't be solved as the Spanish government does, giving money to developers



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to build things that are good for nothing. All workers having left the building branch need to turn to anything different and this has a very high correction cost. A fourth and very important imbalance is unemployment, which in Spain creates permanent imbalance. A 47 or 50-year-old unemployed with a life expectation of eighty years means they have thirty years left doing nothing as they can't be retrained.

«The solution given to counteract imbalance was creating an even bigger one: demand for more megalans for governments.»

The crisis has apparently meant an increase in the number of countries reaching a common base for setting the rules of the game in the international economy, the most significant example being the enlargement of the G-8 to G-20. Nevertheless, there are people saying that in fact we're making for a G-2 consisting of the

United States and China. What do you think of that?

I think the most important is the G-1. In the last G-20 document there is not one single measure talking of common coordination of finance regulation involving all. The **World Bank** is an organisation in which the US and Europe place their money and poor countries receive it from. If China or India want to be present there, they'll need to pay. The United States will go on doing what they want. In fact, Obama is saying the same Bush did, although it doesn't seem so because he says it with a smile in his face.

As one of the main authors of the competitiveness report published by the **World Economic Forum, what measures would you recommend to Catalonia and Spain to improve their competitiveness?**

First of all, they should read the definition of competitiveness. In poor countries it means to produce cheaper, but this dies out with time and then you need to innovate and do things differently from the rest. However, we must not confound innovating with doing research and development (R&D). Innovation means to implement new ideas in business, and these ideas need to come up in all branches, not only in ICT or biomedicine. For instance, three big innovations in recent years came about in the coffee industry with Nespresso and Starbucks and in the textile branch with Zara. This shows that innovation is necessary all over. Building a technology park and trying to lure the best to do research here because the weather in Barcelona is great is just a nice daydream. We need to push the industries where we are good at innovating, but it's not the Catalan government that has to decide in what branches to do innovation. What governments need to do is to set the basis for citizens to have ideas, which means a large reform of the educational system so people innovate and change their mindset. To facilitate this, infrastructures, new laws –right now it's very difficult to set up a business because there is too much paperwork– and a mindset to implement these new ideas are needed. People need to go for risk and not be used to get everything done for them. Also a deep reform of the labour market is needed to



encourage people to work more. Excessive egalitarianism needs to be done away with and those providing more value need to be better paid in order to encourage competitiveness. Finally, the finance system needs to become competitive. It can't be that a country in constant change has a financial system dominated by conservative banks. The finance system needs to be able to finance innovation.

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The R&D budget cut planned by the Spanish government doesn't seem to be a one-off at global level as we could assume, in public authorities as well as in companies. What do you think of such measures?

Those thinking that just doing R&D is enough are wrong. Many things need to change at Spanish universities, like giving incentives, changing the payment system... Nobody has any incentives to work here. A full professor earns €50,000 in Spain, which is slightly more than what a research assistant student is paid in the US. In the US, professors earn much more because there is competition among universities to take the

best, who in their turn attract more and better students. Here you have a minimum wage and no will of doing anything, and this has to change. If you want a good research system you need to start here. This doesn't mean that no money shall be devoted to science. Of course it's necessary, and a lot. But it needs to be managed so researchers are given the maximum incentives to do their job.

Does your long academic experience in the US allow you to state a trend towards a major return of talent to the countries of origin of people educated at American universities?

They will only return as their countries of origin acknowledge the need of giving them what they deserve. Talent is not a country's property, it's a person's. I, for instance, went to Harvard 25 years ago because Andreu Mas-Colell was there. Has it been bad for Catalonia that I didn't come back to teach here? Actually, I don't know. On the one hand, it's true that I teach American students. But on the other, me being here allows many Catalan students to come to Columbia like I went to Harvard because Mr Mas-Colell was there. This way Catalonia has also taken some benefit. Many take advantage of the pioneering spirit, as occurred with Pau Gasol at the NBA. Thanks to him going over there, Catalan basketball is doing very well.



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