

Loanable funds model and current financial crisis essay sample



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The current financial crisis in the United States (and in rest of the world) has resulted to decline in the amount of money available for banks to loan to investors at both individual and firm level. Equally, the situation in the banking industry has resulted to savers losing confidence in banks, which has exacerbated industry woes. Word that current crisis might continue for some time has indeed out the worldwide financial industry at jeopardy. This paper will use the market for loanable funds model to illustrate the happenings in the industry, what stakeholders, especially governments and industrial players, are doing and eventually the effects of the instituted measures on the industry.

The supply for loanable funds is among the affected variables in the current turmoil. Indeed, the declining capitalization in banks means declining funds for that purpose. In this regard, many banks lack the capacity to satisfy respective customers demand. Additionally, banks are not having enough funds to loan to each other, which is resulting to wide range effects across industrial players. The long run effect on this scenario could be disastrous if not brought under control as soon as possible. This analysis therefore argues that government, individual players and collective, as a group should embark on developing solutions to the problem haunting the industry and slowly spreading into rest of the American economy.

Governments around the world have come to understand economic threats posed by the current financial crises, which has resulted to taking measures directed at restoring confidence in the industry. Governments have therefore embarked on having respective central banks play their rightful role as lenders of last result. Additionally, governments of the most affected

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developed nations have embarked on collaborating in the process of controlling the effects in respective markets (NZ Herald). Governments have, however, been keen not to develop solutions that would have negative impact on other economies worldwide. However, individual governments would embark on controlling the effects of the current crisis in their own economies, with hope of protecting locals from effects that could spill over from other countries (Economic Times). Countries are also working towards developing unilateral measures of ensuring reforms in the global financial industry are undertaken effectively. Global financial institutions such as the World Bank and International Monetary Fund (IMF) have hinted on entering into collaborating with world governments, especially helping developing nations deal with the crisis (Morgan; Dratch).

Two major variables are considered in this analysis: demand for the loans by the masses and the supply of loanable funds from the financial industry. The demand variable includes individual borrowers' propensity to get investment funds from the banks. This is in consideration that entrepreneurs and individuals working in industries less affected by the current crisis would need the funds to expand respective operations. These individuals would therefore continue indicating sustainable demand for their services in the market for loanable funds. However, many are the industries tied with the crises in the financial industry and would therefore continue feel the pain of lacking enough financing for respective operations. Other than entrepreneurs, individual Americans would be faced with the challenge of lacking enough finances to fund respective projects such as housing, automobile, and education among others. The effects at the individual level

could be disastrous for the economy considering the large number of Americans affected by the ongoing turmoil.

The other variable revolves around supply of loanable funds as described above. Financial institutions are finding themselves with low funds that can be provided to enterprises and individual Americans. Some of the players in the financial industry have even collapsed or taken over by the government or competitors in a bid to reduce effects on American economy. The unchanging demand for loanable funds while supply is decreasing is putting pressure on the industry and the American economy in particular. The losers in this situation are both lenders (financial industry) and individual Americans; they constitute the economy. The widespread effects have resulted to the government embarking on taking control of the matter.

The Federal Reserve Bank has therefore been guaranteeing individual players in the financial industry. In fact, the government has gone further to providing guarantee of purchasing bad mortgages that are crippling individual banks' loanable funds. The government would then resell the mortgages to the financial industry when the situation improves. It is being hoped that individual players in the financial industry would be in a better position at the time of resale. This is in consideration that companies are being provided with opportunities to restructure, go back to profitability and eventually start their loaning practices. Indeed, industrial players that would be doing well in respective market segments would benefit from re-buying mortgages from the government. Banks that successfully survive the crisis would therefore embark on becoming more competitive in the industry. This

leads to understanding that companies are obliged to reform so as to position themselves better in the industry.

Another variable regards the ability of banks to provide short term loans to each other, depending on individual needs. However, the decline in the available funds among industry players has resulted to reduction in the amounts that inter-banking loans can be provided. Fact that players can hardly come into each other's aid in times of need illustrates complexity of the matter. The hardship of companies being unable to bail each other illustrates the depth of the matter economically and therefore the need for stakeholders including the government and individual players in the financial industry. Such adverse effects on pillars of the American authority would result to the American government, through the Federal Reserve and Treasury Department, been developing mechanisms to deal with the problem. The industry has on its part been collaborating effectively with the government, which has aided in keeping calm as long term solutions are being developed. The American society has on the other hand been patient with the outcomes that are being worked out with the interested parties. The supply for loanable funds is among the affected variables in the current turmoil.

Indeed, the declining capitalization in banks means declining funds for that purpose. In this regard, many banks lack the capacity to satisfy respective customers demand. Additionally, banks are not having enough funds to loan to each other, which is resulting to wide range effects across industrial players. The long run effect on this scenario could be disastrous if not

brought under control as soon as possible. This analysis therefore argues <https://assignbuster.com/loanable-funds-model-and-current-financial-crisis-essay-sample/>

that government, individual players and collective, as a group should embark on developing solutions to the problem haunting the industry and slowly spreading into rest of the American economy. The Federal Reserve Bank has therefore been guaranteeing individual players in the financial industry. In fact, the government has gone further to providing guarantee of purchasing bad mortgages that are crippling individual banks' loanable funds.

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In conclusion, Some of the players in the financial industry have even collapsed or taken over by the government or competitors in a bid to reduce effects on American economy. The unchanging demand for loanable funds while supply is decreasing is putting pressure on the industry and the American economy in particular. The losers in this situation are both lenders (financial industry) and individual Americans; they constitute the economy.

The widespread effects have resulted to the government embarking on taking control of the matter. The paper has used the loanable funds model to <https://assignbuster.com/loanable-funds-model-and-current-financial-crisis-essay-sample/>

illustrate the happenings in the industry, what stakeholders, especially governments and industrial players, are doing and eventually the effects of the instituted measures on the industry.

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