Effects on small businesses

Business

The subprime crisis has produced scathing effects to the financial market both in the U. S.

and globally. In the U. S. for instance, small businesses have felt the brutal repercussions of the subprime crisis. Some of the businesses have reported low profits or losses and others have had to close shop due to inability to refinance their mortgages.

The soaring interest rates of the mortgages and the nose-diving house prices have meant that business owners settle their mortgages from the business income. In addition, small business owners with harsh mortgage delinquencies have had to consider paying their business obligations rather than settling their mortgages. This payment behavior is attributable to the high dependency on their businesses to provide for their basic necessities. The combination of high mortgage payments, reducing equity and curtailed refinancing avenues has seen small business owners choosing to protect their source of income while risking loss of their homes due to foreclosures. Furthermore, a gaping hole has been left on the fabric of the banking industry resulting into a reduced volume of credit available to the banking institutions. This has discouraged the banks from lending particularly to small business enterprises.

Small businesses that need some startup capital or expansion capital are blocked due to lack of enough capital bases in the banks. The high-risk nature of small business, especially in an inflated economy and limited credit in banks results into high interest ratesthat limit borrowing hence discouraging small business ventures. In addition, the liquidation of private

label assets has robbed the U. S. economy and financial markets of a robust liquidity that cannot be restored by the banking system.

SolutionsThe mortgage crises lead to a financial crisis that spilled over to other giant economies like Germany and Japan thus fuelling their economic turmoil (Reinhart, 2008). This is attributable to the intertwining of most nations by globalization and innovation. Therefore, the U. S. government resorted to addressing this unfortunate blunder in her economic history.

One of the major solutions has been the economic stimulus package which has been characterized by income tax rebates that are mailed to the taxpayers. The first of this was the signing into law, on February 13th, 2008, the 168 billion dollars economic stimulus package by the Bush administration (Aversa, 2008). This move was seconded by an Obama administration’s 787 billion dollars stimulus package on 17th February, 2009, accompanied by tax cuts and a wide spectrum of spending. More than 75 billion of this money was allotted to Homeowner Affordability and Stability Plan aiming to assist struggling homeowners (BBC News, 2009). Moreover, the banks who suffered the most in this crisis have been given a boost by the government to increase their capital base. The banks have also acquired solvency through capital obtained from private sources.

Private investors and the U. S. govvernment have also resorted to purchase “ toxic” or “ legacy” assets (mortgage-related assets) from banks with the aim of recapitalizing them. Another way in which the U. S.

government has boosted the capital base of the banks is through the passing of the Emergency Economic Stabilization Act (2008) which incorporated 700

billion dollars to banks which in turn give a dividend-paying preferred stock. Furthermore, some of the institutions considered merging together thus combining the rest of their capital bases. Last but not least, legal and judicial responses have been put in place. This has included litigation and law enforcement processes such as FBI investigations that seek to unravel the fraudulent behavior of mortgage financing institutions like American International Group, Fannie Mae, Lehman Brothers and Freddie Mac. The FBI has assigned more agents in this segment of their profession. The Obama administration has proposed some regulatory measures and long-term solutions.

Some of those them include financial cushioning the banks, consumer protection and shadow banking system regulation expansion. Conclusion The above solutions have however drawn sharp skepticism from various quotas. Financial analysts, the media and economists are divided over the plausibility of the various approaches given to this nagging situation. As this issue continues to elicit debate among federal legislators and regulators; industrialists and lenders, the proper solution still remains elusive.