Good wisdom of implementing austerity measures during the great recession essay e...

[Parts of the World](), [Europe]()

Introduction

The great recession is believed to have started toward the end of 2007, and affected most economies. This was dubbed the great recession in the literature since it was mainly deep and prolonged, and therefore was regarded to be the worst recession since the great depression of 1930s. For years, the economists have not agreed on the causes of the great recession nor have they agreed on the correct policy response to the subsequent recession. This made several governments introduce significant stimulus programs in an attempt to reduce the economic impact of the recession. Similarly, the increase in government expenditures led to increasing budget deficits and public debt, which made governments recognize the need of developing fiscal plans aimed at restoring balanced budgets. However, achieving the objective proved hard in the absence of a sustained economic recovery, and presence the European sovereign debt and banking crisis. As stimulus measures gave way to austerity programs, a policy focused on reducing expenditures and restraining public sector compensation. Several countries were expected to implement the austerity measures with wisdom in order to recover from great recession. Therefore, the paper will evaluate the rationale and wisdom of implementing austerity measures during the Great Recession.

Causes of Great Recession

The causes of the great recession, help understanding why the austerity measures were implemented in various cases. This argument indicates that the great recession was not a failure of free markets, but an example of the

undesirable consequences of government involvement via both expansionary monetary policy and other misguided policies, which aimed at alleviating the problem. In order to prevent a 1930s crisis, economic policymakers throughout the globe, including the United States and countries in the EU among others enacted austerity measures to offset the crisis created by Wall Street (Arestis and Theodore 54). These measures included financial bailouts such as monetary policies that reduced central bank controlled rates close to zero. Others policies include large-scale fiscal stimulus programs which were financed by significant expansions in central government fiscal deficits.

The Significance of Austerity Measures

The significance of austerity measures in great recession. Austerity is the term used to describe debt-reduction policies, but can mean radically different things. Many economies attempting fiscal consolidations, such as Euro zone countries have found that authority measures have hit a growth harder than expected. For instance, in 2010-2012 the growth performance of these countries generally lagged than that of countries such as the US and Germany which did not use significant fiscal tightening. For countries to implement the austerity measures effectively, they need to understand the size of the multiplier. This is so because the size and impact of multiplier changes depending on how stressed the financial sector is and whether the economy is in recession or expansion. These gaps in the understanding of the fiscal multiplier appear to be a principal reason that policymakers have

underestimated the devastating effects of austerity policies in various countries.

Austerity measures in Europe

The effectiveness of austerity measures in Europe depends on the fiscal multiplier. In order to understand the impact of multiplier, we will investigate the wisdom of the fiscal austerity in Europe. This is extremely vital because prior the recent hysteria at fiscal tightening, the fiscal stimulus was thought to be the effective macroeconomic tool to save Europe from another great depression. The attempts made by European and other countries in the world managed to contain the severity of the situation, which would result in a severe great recession. The fiscal multipliers are extremely relevant in the European countries, which have withdrawn their stimulus measures in the effort to regain market confidence (Cynamon, Steven and Mark 6). Implementation of austerity measures in Europe. George Obsborne, the UK chancellor who in 2010 announced drastic cuts in the government budget, proposed the austerity policies in Europe. This was an ostensible effort to avoid the possibility of another Greek-style technical default. His move coincided with the outcome of the June 2010 G20 meeting deliberations that declared support for fiscal stimulus and focused on the risk of sovereign debts getting out of control, despite president Obama's negative reaction. For instance, in the United States case, cuts are happening in a situation where the politicians seem to be incapable of directing average stimulus in productive directions because too much of a stimulus was inefficient tax cuts. Therefore, this US case raises the question whether countries need

more and cautiously directed stimulus to allow the global economy to retain the current economic activity or whether they need a fiscal solution (Arestis and Theodore 55).

The impact of Austerity Measures in Europe

The impact of austerity measures in the sovereign debt crisis. Austerity based on government spending cuts, output and income causes unemployment to increase, tax revenue to fall and sovereign deficits and debt to increase which triggers further financial stress. Despite downsizing government spending, the entire economy shrinks due to government spending cuts. Similarly, if the government responds to economic decline with further spending cuts, the negative spiral accelerates. The sovereign debt of many nations has increased since the great recession of 2007, in response, from 2008 and 2009, the EU and United States governments bailed out banks, and enacted monetary easing and massive stimulus packages via tax cuts and increasing government spending.

Therefore, the rapid debt increase in Europe increased risk and therefore the interest costs on some European sovereign bonds. These higher premiums caused increasing borrowing costs, leading to a further rise in debt, a spiral that finally generated debt crises in the Euro zone, especially Greece. Those crises revealed the vulnerable connection between sovereign debt and financial market stress, which contributed to rising debt costs. Similarly, the increasing costs had a negative feedback effect that in turn increased market stress. Therefore, these vulnerabilities and resulting a significant threat to the Euro zone are significant issues that threatens the future of the

EU (Arestis and Theodore 56).

The recent move to support austerity measures in most Euro zone countries marks an unfortunate sudden turn in the situation regarding the future of EU economy, especially on weaker member states. Europe is perplexed about the sudden drop in support of the fiscal stimulus and focus on the threat of vast sovereign debts and increased fear of high inflation. For instance, since the Greek Debacle on May 2010, most European governments announced drastic cuts in government expenditure in an alleged attempt to avoid the chance of a Greek style of technical default. Therefore, this has led to new developments in the Euro zone where Italy has to renew Euros 120. 85 billion in bond obligations and another dose of Euros 104. 22 billion in treasury bills (Pollin 7).

The Effect of Austerity Measures in Euro Zone Countries

The Euro zone countries adopted strict fiscal austerity, which has enabled their economy to continue to recede and strain their growing health care systems. Similarly, there is an increase in suicides and outbreaks of infectious disease in these countries because the budget cuts have restricted access to health care. Although the great recession poses threats to health, the association between fiscal austerity with economic recession as well as feeble social protection is what seems to increase health and social crises in Europe. Therefore, the austerity measures can worsen the short-term public health effect of economic crises (Karanikolos and Et al 2).

There are debates why this sudden emphasis on austerity measures in countries with a powerful balance sheet given the fiscal stimulus has been

the best policy in times of recession. This is so because if state budgets are controlled, this will reduce the debt because sovereign bond prices are expected to increase and rescue imperiled banks. Meanwhile, the austerity measures will revive Moribund Interbank lending and government-borrowing costs will decrease as well as reinvigorating economies. The embrace of austerity measures is easier to understand in a political context, which is a major issue in Europe. This is so because European politicians are incapable of directing stimulus to productive public investment, which make public to continue rejecting tax increases to cover the future deficits, which today's stimulus would create.

However, the problem of embracing the austerity measures increases the risk of dread outcomes in Europe. These risks include a decline in GDP, sovereign default, political instability and crisis in the capital markets. The dreaded consequences of austerity measures increase the chances of bank failures. The critical question is whether Europe need to direct spending to retain the current economic activity or whether it needs to end the stimulus. Most economists are for austerity measures because Europe is in a position to sustain post secondary education, investment in clean energy and new transport infrastructure among others. Similarly, deficit hawks suggest that self-imposed austerity measures, commencing immediately are the only effective policy choice to alleviate the sovereign debt crisis. Although the United States, commentators are criticizing the Greece situation, the state and local governments throughout the nation are imposing significant cuts in health, education and social services because of the adverse decline in the tax revenues. For instance, the state of Washington is increasing premiums

up to 70 percent for its health plan to serve low-income citizens while California is cutting health care subsidies for about 1 million children. The Americans situation can deteriorate further if the federal government adopts an austerity budget, which includes further revenue sharing for states and municipalities (McKee 346).

Conclusion

In a recap, the ongoing incorporation of austerity measures in the Euro zone has contributed drastically to the poor economic performance of the region. For instance, in terms of the sustained increased in the unemployment rate, it has reached more than 12 percent in 2013. Most economists expect the economic outlook to remain depressed for the foreseeable future giving rise to the chances of a lost decade. The gains that are expected to be achieved from the austerity measures continue to fritter away in deepening and lengthening of the economic recession. The bottom line is that austerity measures can successfully reduce a debt to GDP ratio. However, the problem is that during the period of crisis, policymakers get carried more by politics than by appropriate public policy. The current policy is incapable of ensuring Europe that market forces will be sufficient to restore economic activity after the great recession. Therefore, Europe case indicates that proper implemented of austerity measures can reduce the sovereign debts that have affected the state's economy since the great recession.

Works Cited

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