Free argumentative essay on financial crisis- who to blame

Education, Discipline

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Introduction

Financial crisis has become a global issue because it has affected many countries in the world. It is important to understand its meaning in order to know how it has affected the economy of various countries. Financial crisis is a situation in which the financial assets in a country loss value. During this period, the currency becomes unstable (Irving 2009). In this situation, the country becomes affected adversely because financial problems become unbearable for most investors. The main reason for this is that there are no foreseeable returns from the investments made in the country due to hard financial times experienced.

Financial crisis mostly affects the financial institutions in the country. Financial institutions have the role of enhancing the flow of money in the economy. If this flow is distorted, savings and investments will be affected adversely. If these institutions do not get the required financial aid from monetary authorities, there will be limited circulation of money in the economy. The presence of financial crisis causes havoc in the banking

sector. This is because they fear the risk of closing down due to financial difficulties.

Main Argument-Regulation is to Blame for Financial Crisis

There have been mixed ideologies about the factors that caused financial crisis. This has come from various financial analysts who have studied the financial institutions and their policies. Some of the people argued that this form of crisis took place as a result of deregulation. By reviewing various empirical sources touching on the financial situation in countries, this argument can be opposed. Firstly, it is important to understand the meaning of regulation. This is a situation where there is some form of control from legal authorities. Regulation also involves the formulation of certain policies that help in governing the financial activities in a country (Charles 2008). Deregulation is the process by which the legal authorities remove some or all barriers placed on business and financial activities. Deregulation may also entail reducing the tariffs placed on various activities undertaken in the economy of a country.

In 1970s, financial crisis was brought about by poor formulation of the fiscal policy (Niall 2011). Fiscal policy involves making changes to the taxes and the level of government spending. If these are not matched effectively, then serious implications can be realized in the economy. This happened in Britain, where the fiscal policies enacted led to bad regulation. At some point, the tax rate became higher than expected. This affected people adversely, especially the low income earners. Poor policy planning contributed to ineffective regulation in some countries, therefore driving

financial crisis.

The monetary policies are also important in enhancing regulation in a country. Monetary policy involves controlling the amount of money that flows in the economy. The level of money supply was also used to moderate the level of interest rates. At times, the money supply was relatively low. This led to an increase in the interest rates. At high interest rates, banking sectors could not get many borrowers to enhance increased capital. At this level, there are few investors willing to borrow funds due to the high cost of borrowing. The reduction in the level of investment slowed down financial activities in countries.

Complex forms of regulation also affected the financial position of some countries. At some point, Central Banks enacted monetary policies that were detrimental to the economy. For instance, the interest rates were set at a lower rate. This was held as long as the prices of assets were down. However, if these prices were up, the monetary authorities would not change the level of interest rates. This was to avoid some form of inflation that was in the minds of the public. This form of monetary regulation was not effective simply because it did not include major commodities like food and housing (Niall 2011). Housing facilities are important in enhancing borrowing from the financial institutions. Energy prices were also not taken into consideration.

Regulation regarding housing facilities also contributed to the financial crisis. US authorities designed a regulation that was meant to increase the number of people who owned houses (Irving 2009). At this time, there were many people who did not own houses. This was mainly because there was a large

portion of the population which consisted of low income earners. The regulation gave room to some form of sponsorship to the people. The banking sector was highly affected due to distortions that were brought about in the mortgage market. As a result, mortgage holders ended up making bets on housing facilities that were not protected from risk.

The regulation problem was also experienced in China. The Chinese currency was not stable at some point. For this reason, the government held a series of meetings with the financial leaders in the country. After making wide consultations, the government sought to set monetary policies that would maintain a favorable exchange rate. The major intention of the Chinese government was to prevent the exchange rate from appreciating. Therefore, it spent huge sums of money to achieve this objective. Part of this money was provided by the US government in form of debts. This led to the lowering of the yields of securities prevailing in the capital market (Niall 2011). There is a close connection between the yields of securities and the mortgage yields. This combination led to inflation of property commodities in the country. This contributed to the financial crisis.

Regulation in the banking institutions had severe implications in the economy of many countries. For instance, some Central Banks set a relatively higher reserve ratio for the banks. This implied that the level of reserves held by the bank were high. As a result, banks were left with little cash to offer for borrowing (Irving 2009). This shows that the capacity of the bank to offer credit is determined by the monetary authorities. The tough regulation held on them reduced the level of credit creation in the economy. This led to lower circulation of money supply, leading to lower levels of

investments in the country.

During 1980s, regulation in many countries was faced by disruptions from political scenes. There were regulations made by the then authorities regarding the existing financial operations. However, many political leaders interfered with the set regulations. This led to lack of consistency in the financial market (Fratianni 2009). In most government, there was some form of opposition made from the opposition parties. The opposition side had their own proposals regarding the execution of financial matters. The politics placed on the set regulation caused disruptions, which caused uncertainty in the financial market.

Some of the monetary policies were used inappropriately. Central bank uses instruments such as open market operations, selective credit control, reserve ratios, bank rate policy and interest rates to control the amount of money circulating in the economy. In some cases, the open market operations did not work well. This is simply because the yield set on the government securities was not effective to drive growth in the economy. In addition, operation of some of the instruments used by the central banks was in the hands of some corrupt officers. This affected the movement of financial activities in the financial market, thereby driving financial crisis.

Excess regulation has also been cited as one of the factors that contributed to financial crisis. Base II Accord shows how excess regulation creates an impact in the financial market. This accord encouraged banks to have huge capital, especially when the risk was high. When capital is at a lower level, there will be reduced borrowing in the financial market. As a result, there will be less amount of money flowing in the country. This creates a potential for

the occurrence of financial crisis.

Some of the regulation that had been set in the past did not incorporate fraud detection mechanisms. For this reason, there were a number of cases of frauds reported in some banks. Some frauds involved the coordination of bank employees and other external parties who had knowledge about the operations of the banking systems (Fratianni 2009). Manipulation of accounts was done by certain employees with the intention of getting additional income from the banks. This affected the liquidity of the bank. Eventually, the financial system was also affected, giving room for financial crisis.

In the 1980s, the regulation framework did not conform to the then innovation in the financial market. Shadow system of banking was gaining momentum during this period. However, some banking systems did not adopt this system since they had not been given the right to do so by the regulatory bodies. In some cases, laws relating to the financial markets changed from time to time. This created some form of panic to the banking sectors due to the uncertainty experienced in policy formulation.

Financial analysts argued that regulation on capital requirements was ineffective. In most cases, these requirements were set at a lower level, which was inadequate to enhance financial stability in the economy (Charles 2008). Banks should have a high level of capital to improve its financial position. If such requirements are at a low level, banks may be faced by financial difficulties when the country is in the period of recession. Therefore, a higher level should be set to enable the banks to resist adverse changes in the economy.

Conclusion

The monetary authorities of various countries should strive to ensure that financial crisis is prevented. A history of the past occurrence of the crisis should be studied in order to gain experience in solving financial problems. The employees working in the monetary institutions should be competent enough to enhance sustainable policy formulation. The level of regulation set should be sufficient enough to enhance economic stability in countries. Finally, monetary authorities should institute effective controls that enhance suitable levels of credit creation in the country. This will enhance stability in the financial market, leading to global financial revival.

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