Current economy and the great depresson

Finance

ASSIGN BUSTER

Current Economy and the Great Depression The Great Depression of 1929 was one of the worst economic periods in the world. The US had been experiencing prosperity and optimism for a decade, which propagated lending by individuals with the purpose of investing in the stock market. The stock market crashed on 29 October 1929, causing the worst economic crisis ever in the world. The stock market prices began declining until 1932, by which time they had lost 20% of their initial value in 1929. Besides the effect of the slump down on private investors, many financial institutions began experiencing strains, especially those that held stocks in their finance portfolios (Dent, 2010). As a result, half of the financial institutions in the US became insolvent. In summary, the US manufacturing production was down 54% in 1932 as compared to 1929, while the unemployment level were up by more than 25%, or more than 12 million people. The economic downturn soon spread to the rest of the world due to the relationship of the US with the Europe’s economy in the post World War 1 period. The major reason for the occurrence of the great depression was the deregulation in the banking industry especially in the US Securities and Exchange Commission. Today, the world is facing an economic crisis, which has been persistent since the great recession of 2009. The financial crisis is a result of an extensive credit-fueled bubble that preceded the economic boom of the late 1900s and early twenty first century (Eichnegreen & O’Rourke). The two economic periods have some similarities between them. In essence, the Great Depression and the current economic status occurred after periods of excellent economic growth, productivity, investment, and booms. The Great Depression was a result of extraordinary growth of the economy in the US resulting to the over-optimism of growth in the stock market. Individuals were investing

heavily on the stock market, while at the same time overstretching credit services (Parker, 2007). The impact of this was that financial institutions began offering credit services, like mortgages, even to individuals who were not able to repay. This was the cause of the insolvency of many banks. Similarly, the current economic situation began shortly after 2001 in which the economic growth was significant. What followed the economic growth was ungrounded optimism and over-speculation in real estate market. In government's effort to change credit regulations that would favor economic growth, the Glass-Steagall policy was changed in the 1980s (Dent, 2010). The result was a build-up of subprime and stable mortgages, divided up and sold to spectators. However, most of these mortgages had bad loans, triggering the housing crisis that led to the great recession of 2009 and the current financial crisis. Another similarity is securitization. The effect of securitization was a driving factor for the US financial system domino effect during the Great Depression era. The same factor, though not in an ultra-modern shape and form, was a factor that has contributed to the current economic situation through dicing and slicing of tranches and pools of seniority. Excessive leverage was a driving force for financial pains and liquidation during the late 1920s. Analyzing the 1930s situation, it is clear that the problem was not the deleverage process, but rather the excessive leverage that occurred before the deleverage process. In similar manner, the 2008 deleverage process was a factor that led to these economic problems. The investment pools of the 1930s and the current Hedge Funds are similar in cause and nature (Dent, 2010). Corruption of the gatekeepers in the 1930s, the Worldcoms and Enrons, through the abetting and aiding by accounting firms resulted in profits on their sides. The companies were the

gatekeepers of the financial system at the time, neglecting their responsibility of watching over the activities of the financial market. The same lot of gatekeepers is also responsible for the current economy resulting from their overvaluation of real estates. Another similarity between the Great Depression era and the current economic status is the market ideology. In the late 1920s, the financial market was for the idea of “ laissez faire” or market fundamentalism. The idea of free market works best, but the ideology is not applicable in the money market as the Fed (and other central banks) is responsible for the control of the value of money. The implication of this fact is that the central banks can maintain the value of money long enough to clear the imbalances in the financial market without imposing discipline to the market (Parker, 2007). These measures may lead to the sort of problems that the economy current economy faces. Government intervention policies in the two economic times are also similar. The ban on short selling in 2008 and the current period are similar to those that were imposed during the early stages of the Great depression (Eichnegreen & O’Rourke). The government also provided stimulus packages for the economy during the Great Depression, same as the provisions of the same during the current economy. In conclusion, over-speculation and deregulation in the credit market are the leading factors to both the economic downturn. The effects of both were massive unemployment rates and increase in the living standards, in the US and all over the world.

References Dent, H. S. J. (2010). The Great Depression Ahead: How to Prosper in the Debt Crisis Of, 2010-2012. New York: Schwartz Publishing Pty, Limited. Eichengreen, B. & O’Rourke, K. H. A Tale of Two Depressions: What do the New Data Tell Us? Retrieved on December 1, 2011, from http://www.

voxeu. org/index. php? q= node/3421 Parker, R. E. (2007). The Economics of the Great Depression: A Twenty-First Century Look Back at the Economics of the Interwar Era. Cheltenham, UK: Edward Elgar Publishing Limited.