Economic recession

Economics

The economic literature on the current recession is still limited, however adequate amount of literature exist on the impact of the down turn on the U. S. economy. The Economic Report of the President Jan, 2009 gives a comprehensive coverage of how the recession started; where it started and what is to be done. A large amount of literature can also be found on the causes of the crisis. among others. In terms of impact, the reports from the Bureau of Economic Analysis (BEA) indicates that from Dec 2007 to May 2009, America has had 57 bank failures; the unemployment rate has increased to 8. 9%; the economy has declined by – 3. 3% from the second quarter 2008 – first quarter of 2009; from Sept 2008 to may 2009, the federal government has increased themoneystock by 125% and over the same period the biggest fall in the Dow Jones industrial stands at -53. 8%.

The outlook is equally dire; most analysts have predicted a recession that may last up to two years (Roubini, 2009) Moody’s Investors Services (MIS), while further job losses are also expected have predicted increased foreclosures, while further job losses are also expected. But the impact has not been limited to America.

The International Monetary Funds (IMF) World Economic Outlook published in Jan 2009 painted a bleak picture of the world economy in general: They predict that the real global growth will be close to zero; in the same report, growth in advanced world economies was projected at -2%. In his report, presented to the V Symposium on International Trade (Feb 20, 2009) Cline reported that the economic crisis in America has triggered a highly synchronized global recession, which has seen a contraction in all economies (see the Graph below showing global growth over 3 decades (Cline, 2009).

Taken together, commentators are unanimous that, in term of severity, this recession is still mild vis-a-vis TheGreat Depression. Shiller (2009) writes that a lot of the upheavals in the economy have not been seen since the GreatDepression. He cites the stock market volatility, the bank failures, the housing bust, the breakdown in intermediation, and the near zero interest rate. Besides the statistical comparisons, the current debate and research effort is focused on how the how the crisis started.

The proximate consensus is that: the mortgage security backed housing boom in America it to blame and that the origination and distributions of this paper assets is at the heart of the problem (Markus; 2008; Grotty, 2009; Bernanke, 2009; Gapper, 2009) at the same time, researchers maintain that the crisis in the banking sector, was not independent, but resulted from distortions and incentives created by past policy actions.

Blundell-Wignall, etal (2009), in there paper presented at a Reserve bank of Australia conference, averred that the current financial crisis is caused by global macro policies affecting liquidity and by very poor regulatory frame work. More specifically, economists recognize that any theory of causality, must, among other things, explain how the housing boom started, describe the factors behind the explosion of the residential mortgage backed securities (RMBS), how the banking crisis was triggered and the policy distortions that made it possible (Tett, 2007; Rajan 2009; Grotty, 2009).

The findings of a number of researchers who have studied the causes of the current financial crisis in America conclude that the policy distortions started with gradual undermining of the Glass Steagall Act, from the 1980s; and the rise of the neo-classical theory of free markets (which advocates markets deregulation) Shiller (2005, p 43) argues that business cycles in the financial markets would not have been a major problem had banks been kept off the asset markets. The same argument is advanced by Summers (2008) who asserts that the deregulations in the banking sector exposed the banks to the bubbles and bursts of asset markets.

Wray (2009) traces the poor regulatory framework in the U. S to the New Financial Architecture (NFA) which he claims is represented by a globally networked system of giant bank conglomerates and shadow banking system of investment bank, hedge funds and bank created special investment vehicles (SIV). In short, most scholars agree that the Riegle-Neal interstate banking and Branching efficiency Act of 1994 and the repeal of Glass Steagall Act in 1999 through the Gramm-Leach-Bliley Financial Act played a crucial role in laying the foundation which led to this crisis (Mishkin, 2009, p 268; Grotty, 2009).