Sub-prime mortgages more to blame for the current crisis

We can easily conclude that the credit default swaps crisis stems directly out of the inability of creditors tofinancetheir loans. The mortgage defaulters have significantly impacted on the buyers of credit default swaps such that they are in a deep economic plunge. The severity of the economic affliction has led to uncertainty such that the losses incurred may be too much for the CDS counterparties. The net worth of financial institutions continue to deteriorate as a result of losses from sub-prime mortgages such that CDS buyers have to cover for the defaults (Gilani, 2008).

Uncertainty looms as investors become worried about who will pay for the defaults. Insurance companies which are the major undertakers of CDS face potential danger of closing down. A good example of this is the American International Group (AIG) which had to pay numerous mortgage defaults out of the $440 billion it had insured in CDS and in the end the company had to obtain a bailout from the government to help in reviving its activities (Gilani, 2008). Canadian banks are also said to be fighting with CDS worth more than $800 which they are not sure if they are going to be repaid (Hasselback, 2008).

As financial analysts come to their conclusions on the current economic crisis, it is quite obvious that the mortgage sector has played a major role in fueling the crisis. However, the debate does not end there; analysts still insist that poor government regulation is the sole cause of the recklessness witnessed in the mortgage firms and banks in a bid to make more profits (Yuliya and Hemert, 2008). Now that their speculation has turned against them is the major concern in this contentious issue.

Default in repayment of loans continues to cause a chain of problems: the banks have to reduce on their lending because their reserves are diminishing; investors cannot access loans to expand businesses; businesses relying on loans to cover for their expenses are being declared bankrupt; with closure of firms, the employees are losing their jobs leading to decrease in disposable income (Ghosh, A and Ghosh, C. 2008; Knoop, 2008). At the same time, the government's income through tax revenues is dwindling pausing a danger of deficit budgets.

There can be no worse economic crisis than this and as Krugman (2008) notes, the ability of a country to develop is highly curtailed by unavailability of funds and more so credit. Finally and in a bid to revive the failing financial sector, the federal government has resulted to bailing them out. Bailing out has been criticized as a way of transferringmoneyfrom the poor who are already suffering enough to the rich who actually caused the crisis thus creating heated debates within the country (Yuliya and Hemert, 2008).

Conclusion In the height of the current economic crisis sub-prime mortgages stand out as one of the major causes of the crisis. Its bad news that many credit default swaps are written on sub-prime mortgages which have nothing much to show other than foreclosures leading to the high rate in mortgage loan default. The credit default swaps too are threatening financial crisis and in the wake of the current global situation there is need for the government to intervene to prevent these future fluctuations in the finance market.

Otherwise, there is still fear that the world could go back to the era of thegreat depressionleading to high interest rates and unemployment levels

(Krugman, 2008). Dealing with a credit crunch is one thing that could highly curtail the development of any nation due to the unavailability of funds to investors who highly rely on banks for their finances. The major challenge now lies with the government to control the private sector which is already threatening to push the economy into a downward slump. Policies such as contractionary monetary policies and bailout policies could prove effective in solving the current crisis.

Co-operation between the government and the private sector should however be emphasized to ensure bailout funds bring in a positive value. Regulation should also be heightened to promote safer business practices. Word Count: 1862.

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