Austrian Economics and the Financial Crisis of 2008

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Abstract

This article analyses where Austrian Economics find the origin of the current financial crisis and what will be done if economists adhered to Austrian economics. Previous research shows that there exists an argument by Austrian Economists of having theories that predicted the crisis and solutions that are fundamental in curbing the crisis. Due to the criticism from mainstream economists, however, this article shifts focus by instead analysing the existing literature and the credibility of both the Austrian economics and neoclassical economics. The approach taken is critical analysis of the existing theories from both groups of economists. The results showed that neither side is wrong in their argument but there exists a significant correlation between the two groups of economists. The conclusion is that Austrian economists have a stronger argumentative point since most of their theories are fine reviews of the mainstream economics. This paper implies the need for integration of the two economic sides and provides the researchers and readers with a detailed view of the Austrian economics in relation to the financial crisis. It goes further in providing the relevance of the integration of Austrian and mainstream economics.

Keywords: Credit, Banking, Austrian Business Cycle Theory, Mainstream economists and Praxeology.
JEL Classification: E50

Introduction

Background of the Study

Reportedly, the global financial crisis started in the year 2007 into the year 2008. Economists and researchers claim it to be the worst economic recession since the Great depression of 1930s. It started with the bursting of the housing bubble in the USA and has now influenced almost all economies of the world (Crotty, 2009). This essay identifies the actual causes of the global financial crisis with perspectives from various Austrian Economists as well as other economists who have given a range of theories concerning the financial crisis. It goes further in analyzing the impacts of the crisis on the global trade and more specifically on the Austrian economy.

Many of the Individual economic theories given about the financial crisis do not offer a complete overview of the crisis itself. This article has integrated various theories in order to come up with a clear interpretation of the financial crisis on a wider perspective. In the initial stages of this paper, a detailed description of the 2008 crisis will be provided in an assessed manner to provide an insight on what could have actually ignited the financial crisis. From a dictionary definition, an economic crisis is a worldwide problem that arises when the consumers and investors start losing confidence in their financial systems and financial institutions (Nanto, The Global Financial Crisis: Analysis and Policy Implications, 2009). It is also a time when many prominent financial institutions as well as superior governments get into bankruptcy and lose the credit worthiness influencing the many economies of the world. Besides these crisis starters, the paper will also try to disentangle more financial "shocks." Some of the sources of the financial crisis have not been given so much weight in many existing economic theories.

Despite looking at the sources of the financial crisis, this article has with so much weight analyzed where Austrian Economists find the origin of this current crisis and what will be done if all economics adhered to Austrian Economics/and or in reality. It gives an in-depth analysis of the many concepts and ideas offered by Austrian economists and the many recommendations offered to these ideas. Some of the Austrian economists have publicly criticized some of the mainstream theories claiming that they are not practical. This paper critically looks at the Austrian Business cycle Theory (ABCT) that has been claimed to be one amongst the most authoritative theories, which analyze the financial crisis of 2008 in depth (Khandker, 2011).

Statement of the Problem

Austria is a country with a well-developed economy and is considered the 12th richest country in the world. This is based on the Gross Domestic Product per capita (Krieger & Crahan, 2001). It joined the European Union in 1995 and its economy comprises a highly developed agricultural industry besides other large industrial businesses. The story about Austrian School of economics goes back into the fifteenth century. Various scholastics have over the years given many economic theories via the Austrian School. Laws of supply and demand, inflation, exchange rates are some of the theories developed in the Austrian school of Economics (Woods, 2005). They use an approach known as Praxeology, which involves deriving economic theories logically using human action. They are known to be critics of economic models and statistical methods used by many mainstream economics. They have been segregated in a minority position because of their rebellion on mainstream theories. However, some mainstream economics are still borrowing from them including the subjective theory of value and theories of marginal utility. Many Austrian approaches differ from the approaches used by the mainstream economists. In this regard, the Austrian economists have tried to give support on why they think their approaches are the best in achieving sound economic systems. They have not gone without criticism from various economists and scholars. Hence, this paper will also highlight on the criticism Austrian Economists have faced and reasons for such criticism. It is a point to note that Austria is considered by many economics as a "lucky country" due to the minimal influence that the global financial crisis had on it. When the impact of the crisis is measured in Austria, it is not comparable to that of other developed countries like United States, Japan and other European countries.

Research Objectives

The general objective of this study will be to determine where Austrian Economics find the origin of the current financial crisis and what will be done if economists adhered to Austrian economics.

Literature Review

An Overview of the 2008 Economic Crisis

The global financial crisis started in the year 2007 into the year 2008. The crisis was based on sub-prime mortgage lending whereby a liquidity crisis arose due to damaged investor confidence in the USA mortgage credit markets. Banks would pool their loans into sellable assets and then pass the risks to their borrowers. (Brummer, Trujilo, Commission, & Ala`i, 2010) The banks saw this as a way of raking in lots of profits and went on taking more and more mortgages so that they could securitize them and give more loans. This led to increased money supply in the economy and pressure was piling up to the borrowers of whether to invest in them or spend on the highly priced commodities such as food and oil (Spahr, 2009). It got to a point where people realized the risk they were being exposed to and lost confidence with the banks. Many banks got into huge debts and this made them insolvent leading them to seek help from the governments. Governments tried to ease their monetary and fiscal policies and this meant a reshaping of the world trade. (Nanto, 2009). One of the earliest effects of the crisis was the collapse of a mid-sized investment bank by the name Lehman Brothers on September 2008. Lehman Brothers experienced huge losses due to overpriced assets, huge unsecured loans and inflationary effects (Schechter, 2011). This did not have a direct impact on the world trade but the effects that spilled over from then have had critical impact on the world trade. These effects have affected the world trade through many channels. Some are obvious while some have been exacerbated from prior effects. One of the most obvious effects was the drop in household spending. This led to a drop in consumption that has triggered the decline of imports and exports. (Spahr, 2009). Another obvious way involved the fear by banks to lend each other because of the risk involved. This meant increase of risk premiums, which resulted in increased cost of capital. Similarly, this had an effect on trade flow. Stocks began to fall while investors traded their equities off affecting the Wall Street.

Businesses started facing a decline and the housing sector even became much worse as the prices continued to rise. The financial crisis was hence felt around the world as the consumers, investors and financial institutions began reacting to economic indicators like inflation, food and oil prices, projected and reported loses by financial institutions especially banks and other reports by economists and commentators around the world. This led to stock prices falling and investor confidence fading around the world, resulting in massive losses especially by banks, mortgage firms and investment banks. The problems in these big corporations made it necessary to cut employment and reduce costs, further triggering unrest and uncertainty around the world. Production levels went down and demand fell to low levels that were not able to sustain economic growth.

The United States experienced the most severe effects from the financial crisis. However, all the countries that traded with the US in a big way instantly inherited the impact. Austria is said to be the sixth largest trader with the US and therefore was not spared the wrath of the crisis. Developing countries are said not to have experienced so much impact especially the African countries. However, in the end the financial crisis has trickled down to all economies of the world. Unemployment rates have shot up, political instabilities, change of pattern in the world trade and unrests are some of the trickled down effects.

Effect of the Crisis in Austria and In Comparison of the Effects in Other Countries

Austria is considered by many economics as a "lucky country" due to the minimal influence that the global financial crisis had on its economy. When the impact of the crisis is measured in Austria, it is not comparable to that of other developed countries like United States, Japan and European countries (Davis, 2008). Therefore, this subtopic has tried to look at the varying impact of the financial crisis on the different countries stated above.

The hard hit countries by the crisis are predicted to have their GDP decline by over 4 %. This involves all member states of The European Union as well as the United States. Austria`s GDP continues to rise despite the effects of the financial crisis. From the year 2003, the GDP of Austria has risen from over 0.8% to 1.4% in the year 2008 and currently it stands at 3.1%. The inflation rate of Unite States and European countries has continued to decelerate to a point of entering negative regions in 2009. They were however able to stabilize a bit as from then with few fluctuations. The Austrian inflation rate is estimated to be 2.2% in 2012 compared to last year's rate of 3.6%. Unemployment rate has been another distinguishing factor, Austria`s rate is continuing to decline while the unemployment rate in European countries and the United States is estimated to rise to close to 11% (Austria Country Report, 2012). The decline is estimated to be beyond fifty percent. Statistics show that the housing price registered by US during the Great Depression has declined more than twice. Austria was amongst the countries least hit by the crisis.

GDP - composition by sector	Source	agriculture: 1.5% industry: 29.5% services: 69% (2011 estimate) *(Data released on February 2012)*			
Gross domestic expenditure on R&D *(% of GDP)*	Source	2.76% (2010) *(Data released on March 2012)*			
Inflation	Source	2009	2010	2011	2012*
		0.4%	1.7%	3.6%	2.2%
		**Estimate*			
Unemployment rate	Source	2009	2010	2011	2012*
		4.8%	4.4%	4.2%	4.4%
		**Estimate*			
Household saving rates	Source	7.7% (Net saving; 2012 forecast) *(Data released on December 2011)*			

Figure 1 Source: (Reinhart & Rogoff, 2009)

Research Findings

Origin of the Financial Crisis on Austrian Perspective

Austrians use the Austrian Business Cycle Theory in providing an explanation on causes of the economic crisis. A fact exists in this theory that when the economy has too much money supply, a liquidity effect may arise. This financial shock leads to market interest rates decreasing beyond the set interest rates (Fett, 2011). The credit market model has the potential of accommodating different interest rates simultaneously both in a short or long duration. However, this may have a negative effect on the investment of housing as well as investments in other capital assets. Consumers tend to spend less given that there are very few incentives to save. Hence, there is an overconsumption of commodities. Since there is very little savings and investment for that matter, the created credit is not enough to finance the existing investments. Consumers and investors realize their mistake and lack confidence with their lenders.

Austrian economists blame the Federal Reserve`s monetary policies on the financial crisis. They argue that the Federal`s move to lower the market interest rates below the artificial interest rates resulted in an unnecessary asset inflation. Banks in their bid to increase their returns leveraged up. They argue that the Fed`s regulation through the credit rating agencies allowed the banks to behave irresponsibly. It allowed them to invest in securities that provided good returns only if the prices of housing sector continued to rise (Fett, 2011). However, the interest rates stabilized back to the artificial standard and housing prices started going down. This resulted in a major housing bubble, which resulted later into a global financial crisis. This blames the Federal Reserve of the US for assuming they had the power to intervene into the economy at any time. Different economists explain the Austrian Business Cycle Theory providing an understandable picture of how it predicted the birth of the global financial crisis. These same theories provide an insight on the practices that can lead to having a perfect economy.

Recommendations by Austrian Economists

Theory of Money and Credit by Ludwig Von Misses

Von Misses provides an insight on the role of money in the economy as well as practices to follow in achieving a sound economy. He insists on adoption of effective and credible sound monetary systems to achieve a stable economy (Misses, 2009). He provides four features of money that should be critically analyzed in order to achieve this objective. Firstly, it is important to identify the value of money and its relationship to the economy. Second, assess its purchasing power and possibilities of economic authorities changing the purchasing power. Also, look at its impact on the economy and social effects if altered and/or not altered by economic authorities. He places more emphasis on the monetary policy. Von Misses emphasizes on money and banking as fundamental features in the economy set-up. Von Misses supposes that money is only necessary when there is an economic order. The exchange between first order goods and second order goods should not be interfered with (Misses, 2009). The central banking system is not supposed to dictate the production of these goods. Lack of disruption in this production as well as proper documentation of the consumption of these goods (Mises, 2009) would result to accuracy in their valuation. This means that their valuation would be based on the equilibrium prices. If this is followed to the letter, money will have performed its function. The function in context is the function of medium of exchange that ensures balancing of the forces of demand and supply. He asserts any imbalance of the forces of demand and supply would certainly result in an economic crisis (Shiller, 2008).

Money has always been used to facilitate credit transactions. We need to understand the meaning of credit transactions to understand the function of money in credit transactions. It refers to the exchange of present goods for future goods. Therefore, the function of money exhibited in this context is the "standard of deferred payment." With the change of real value of money comes the change in the values of debt (Dodoo, 2011). Money as a standard of deferred payment explains the reason for inflation having a negative impact on the economy. The 2008 economic crisis was influenced by persistent increase in prices of commodities relative to the given base year. Prices of commodities were shooting up in the year 2007 leading to an increase in value of debts. Economics claim that prices of commodities had risen more than double. Food prices and oil prices were some of the items that faced a significant change during the crisis (Mises, 2009). This instability in prices was a critical source in the development of the crisis. Financial institutions especially banks were under pressure since the value of debts were increasing simultaneously. Statistics show that the US mortgage debts in the time rose from forty –six percent to over seventy-three percent. People who had taken loans with these banks were also facing same dilemma due to the increase in value of personal debts. It was a challenge not only to private households but to the investment bankers as well.

Mainstream economists have argued that cartels, adjustable flat currencies and deposit insurance are the best channels for a government to control its monetary policy and banking systems. However, Austrian economists assert that private markets are the best channels of ensuring persistent monetary policy and good banking system. The Austrian Economics School has tried to sell this idea to the mainstream economists. In regards to the deposit insurance, the government places taxpayers money as security on its loans and therefore financial institutions tend to behave irresponsibly (Janssens, 2011). Austrians consider the practice of deposit insurance unacceptable. Therefore, no taxpayer money should be used in bailing out insolvent institutions.

Austrian economists argue that it is not the market responsible for the cyclical behavior of an economy rather the central banking system of the country. They support their proposal through analysis of many recessions of the past, which show that the central banking system was responsible. They advice on not ignoring the smallest increases in money and credulity based on their size since they always have an impact on the creation of a business cycle. Many people would then question on what step to take if an economy enters into recession. Some Austrian economists give a highly unexpected answer, "Nothing." However, they claim that it takes so much time and effort in dealing with the impacts of credit booms. Investors have to go bankrupt; wages price decline, unemployment rate increases and many people have to be fired. It is only after the economy has experienced all these that growth can start afresh based on an analysis of the future consumer behavior (Mises, 2009).

The Austrian economists go further in giving proposals on what the governments should do if they wish for a quicker recovery. For example a government may be facing an election in the near future and hence need for a quicker recovery. Some of the suggestions provided include cutting on taxes to maintain a high money supply in the economy (Thoma, 2012). Second, it can loosen the regulations set up for private businesses to enhance investment. Another option may include reducing on government spending and reducing demand on credit markets. It may also reduce tariffs and quotas imposed on imports to facilitate buying of goods from outside at cheaper prices. Since the central banking is to blame for economic imbalances, the Austrian economics propose on a return to a hundred percent gold coin standard. Some even call for the abolition of the central banks while some suggest that the consumers be given a variety of currencies to choose from (Thoma, 2012).

Public Policy

For Austrians, economic regulation is considered a killer of smaller business and prosperity. This is because it leads to misallocation of resources. Environmental degradation is one of the deadliest plagues in the recent years. The losses caused on our wetlands and the general environment cannot be measurable. The Clean Air Acts and the endangered species have all been associated with great losses. However, environmental policy goes on in doing its intended purpose, which is to lower standards of living. Nevertheless, antitrust policy does not generate competitiveness concerning its stated policy. Such a situation scares bureaucrats at justice (Ebeling, 2010). This is because it is not logical for a competitor to sell at a price lower than the cost of production and yet sell at monopoly price in the future. Selling at a price lower than the cost of production automatically leads to a loss. If it dares increase the price in the future, it means inviting the competitors back.

Economic regulation also has another disadvantage. It suppresses the entrepreneurial process. Entrepreneurship requires having a broad area full of business ideas that can be converted to business opportunities. However, environmental regulation initiated by the government impedes the process. Existing production is restricted as well as innovation of new production techniques. Some of the environment regulations that impede the entrepreneurship process include safety and health regulations. Another form of regulation is the civil rights legislation, which influence patterns of hiring, firing and promoting (Ebeling, 2010). Employers cannot carry out these roles based on merit rather there are strict procedures to follow. This leads to dislocations in the organisations as well as the labour market as a whole. Civil rights have also been known to give preferences to some groups in organisation creating unfairness by undermining the public sense of fairness.

Redistribution is another key factor the Austrians criticize, as a way of ensuring there is a sound economy. It is a method used by various mainstream economists though. Based on the mainstream perspective, it is possible to increase the total utility if the law of diminishing marginal utility is true. They point out that you should take a dollar from a rich person in order to decrease his/her welfare slightly. However, that dollar is worth less to him compared to its worth on a poor person. Therefore, the total utility increases by just taking a dollar from a rich man to a poor man. Welfare is attained through perfect income equality. The only problem with this theory though is that you cannot add or subtract utilities because they are subjective. By definition, this theory takes value from the producers and property owners and gives it to non-producers and non-owners. The value of property redistributed diminishes in value. Therefore, to the Austrians it better to avoid redistribution as a way of stimulating the economy. They claim that it even causes more damage to the economy. For example, increasing taxes leads to wealth destruction or confiscation of property that could otherwise have been invested. Consumers' options in entrepreneurship become limited. Austrians assert that all taxes lead to a reduction in production and there is no such thing as strict consumer tax. Many economists claim that deficits do not matter. The Austrians tend to differ with this statement. Their point of argument is that deficits have an influence on interest rates, which increase meaning that investors become disappointed. Many central banking systems tend to increase taxes in order to finance deficits. Austrian economics suggest that governments should practice budget balancing through adopt spending cuts rather than increasing taxes. They go beyond in suggesting that government spending should be a short-term solution because in the end it may lead to diversion of resources from better uses (Ebeling, 2010).

Human Actions

"The future is always uncertain;" is a concept, which the Austrian economists agree with although it is not so radical. We need human beings in confronting this uncertainty. Entrepreneurs are better placed in future forecasting than economists are. However, this does not mean that Austrian economists ignore consequences of various government policies. Austrian economists use "Praxeology" in studying the human behaviour (Rothbard, 2011). Ludwig Von Misses used praxeology in explaining how human actions are used in achieving certain goals and how they make choices that they perceive to provide outcomes that are satisfying. Praxeology theory also exemplifies the free market economics precisely on the perspective of the Austrian School of economics. He argues out that human actions drive the world and always keeps us alive. It is an undisputable fact that the human behaviour is influenced by certain motivational factors. The repeated behaviour of a human being is influenced by the need to achieve some satisfaction and a person will do it until they no longer feel discontented. The actions and in some cases miss-actions of human beings results in creation of markets. When human beings are left to act freely or independently many benefits accrue unlike when there is interference in their behaviour. Austrian economists therefore insist on the independence of human beings in achieving economic success. It is necessary to minimize unnecessary influence by allowing the free interactions of economic agents to create goods and services. Allowing consumers to consume freely is also fundamental. This means that capitalism is the best form of economic ideologies. Von Misses claims that the interference of the human mind is relatively influencing the human behaviour and therefore socialism has an impact on human actions. Socialism instils control and in some cases fear in the human mind that denies them free interaction with each other. This may act as a barrier to economic production (Joseph Conrad's Praxeology, 2010).

Von Misses asserts that human actions present the problem of calculations in economics. What the human mind knows or the information is available is what it uses to evaluate choices. Some information influences the categorisation of choices based on their importance. Priority is based on the need to achieve something and the human mind will try to look for the best ways to achieve those needs. Through independence in free markets, the true value of products is achievable. Entrepreneurs are the best placed people in an economy capable of estimating costs more effectively. The soundness of an economic system is therefore dependent on the actions of the entrepreneurs. How they try to balance an equilibrium in which principles of the economy exist is very critical. Austrian economists blame the 2008 financial crisis on the human actions in a very big way (Rothbard, 2011). There was so much speculation at the time rather than relying on real economic calculations. Bankers were speculating huge profits from the mortgage loans and did not take into account the potential risks available. They went on borrowing more financial assets resulting to an increase in the value of the mortgages beyond their real value. If the entrepreneurs had strong cost allocation systems and did proper economic calculations, none of the consequences faced would have risen.

Time preference is a core cause in how human beings behave. For example, during the 2008 financial crisis bankers borrowed more mortgages with the view that in time, value of real estate would increase. They did not even consider other external factors. Von Misses argues out that human actions are dictated by time preferences that make people demand compensation for the foregone consumption, normally represented by interest. The investors thought that with time they would gain high interest rates while consumers looked forward to higher returns. The bankers expected the consumers to invest in the loans but due to the increasing prices of commodities people opted to spend leading to overconsumption. This sparked the so-called "global financial crisis" just because of improper speculations by human beings. The past also had an effect on how human beings acted during the financial crisis. The capital goods of the past were not adequate and efficient in satisfying the needs of the time. It was the responsibility of human beings to ensure production of better capital goods. The decision by people to spend more rather than invest in production of these capital goods resulted to a shortage of choices. The Austrian economists therefore advocate for low consumption by human beings and increase of investment to ensure continued production of capital goods (Mises, 2009).

Criticism of the Austrian Economists Approach towards the Financial Crisis

Austrian economists have contributed much in the development of the economic world. However, the mainstream economists dominated the economic world even during the financial crisis. Mainstream theories and Austrian theories are considered mutually exclusive. Some scholars saw the Austrian economists as competing with the neoclassical or mainstream economists. This is so unfortunate (Rothbard, 2011). The economic perspective of the Austrians is more evolutionary and human actions represent the main tools of changes in an economy. They are more macroeconomic with much focus on decentralization and competition as key factors to consider when evaluating an economic system. On the other hand, the mainstream economists offer a microeconomic perspective. Austrian economists are criticized as being responsible for transformation of many economic policies to a point. An era of Laissez-faire was created in the world. Laissez-faire is an economic model in which private parties have become free of any government action (Wiecek, 2001). This environment has been related with so many challenges because it has resulted in human beings losing their sense of direction and focus. Mainstream economists argue that it is necessary for the government to intervene in an economy occasionally. Despite Austrian economists claiming that, a free market offers a productive competitive ground for businesses, the neoclassical economists assert that the opposite may be the outcome. Large industries in the private sector are often monopolies. Monopolies if not monitored and controlled by the government may exploit the market through exorbitant prices, low quality products and even poor presentation of their commodities in the market. The government comes in ensuring reasonable prices and facilitating competition in the large firms. Mainstream economists argue out that a free market would expose the freedom at the exploitation of selfish interests. It would allow people to attack labor laws and other regulatory policies laid out. The Austrian economists are therefore most of the times ridiculed for introducing a fantasy economic world that cannot be practical.

There was a time when two Austrian economists argued over the nature of rates of interest (Keizer, 1997) in a very hot debate. Another scenario of such happened when there was a difference of opinion between students of two Austrian economists resulting in their divergence. These were pupils of Misses and Hayek, renowned Austrian economists. Mainstream economists use these two scenarios in showing how bad the reputation of Austrian economists is and they go further in claiming that they were responsible for the creation of Austrian economists. Through the many debates that existed between the mainstream economists and the Austrian economists, Austrian economists were able to develop their own distinctive approaches. They use the neoclassical approaches as foundations for their theories (Augier, 2000).

Mainstream economists question why Austrian economists assume entrepreneurs have irrational expectations. They argue out that entrepreneurs are trained to prevent errors and therefore are capable of handling uncertainties. It is therefore not logic to assume that these entrepreneurs are responsible for all economic fluctuations unless there is interference with the economic systems. Inconsistency on Austrian theories has also been part of the criticism (Keizer, 1997) . When consumption and investor`s preferences re-assert themselves it is unclear why the industry of consumption goods does not face a huge boom during depression. By default, if prices of capital goods increase it means the prices of consumption goods are low. Why do the Austrian theories have different predictions of unemployment in different sectors regards the situation? (Keizer, 1997). They predict of a short term increase during depression yet it`s normally related with a decline in output. This inconsistency is what is bringing controversies in the Austrian theories. The Austrian Theory of the Business Cycle prides itself in explaining why consumer goods industries suffer less than capital goods industries during depression (Soto, 1982). However, mainstream economists claim to have the simplest approach of explaining the phenomenon. In some regards, Austrian theories are said to be the only theories capable of explaining stagflation while there exists numerous theories that have the same role although they were used in the 1970s. However, Austrian theories continue to undergo numerous reviews and are even in collaboration with various mainstream economists to enhance the practicality of the existing economic theories.

Summary

The financial crisis has been dubbed a "global problem" since it has affected almost all economies of the world. Despite the strong policies in Austria`s economy, the economic crisis has had its significant impact on the economy. The impact is considered minimal compared to other countries of Europe and the US resulting to Austria being referred to as the "Lucky Country." However, economists predict a fall in Austria`s GDP as well as decline in their economy if strong consistent measures are not taken up. Global financial crisis has been known to have "trickling down effects" and therefore the Austrian economists need to ensure stability even in other economies of the world. Conflicts continue to rise between the Austrian economists and the mainstream economists on what are the best approaches of confronting the crisis. This tension continues to create instability in very many economies because no one side is being considered the best. Unemployment rates, inflation and public debts continue to accelerate. In this paper Austria`s theories have been analyzed in-depth giving an explanation to the origin of the financial crisis as well as what should be done if the crisis was to be confronted using the Austrian approaches. The paper has gone further in assessing the credibility of the Austrian theories as well as detailing out the given back up to the mainstream economic theories. By providing details from both sides, it makes it easy for the reader to make a systematic comparison as well as a subjective decision. The crisis had minimal effect on Austria and many readers would claim the Austrian economics to be the best based on this fact. However, other readers may argue out that the mainstream economics lay ground for the Austrian economists and therefore mainstream economics stand out as the best.

This paper suggests, there is need for integration between the Austrian economists and the mainstream economists to prevent the crisis expanding not only in Austria but also in all economies of the world. Austrians economists may assume mainstream theories as inadequate but literature is evolving and criticisms may continue to increase in quantity. There is also the need to test the economic theories that arise and Austrian economists do not provide a reason for their testability. The Austrian Economists have a reason to rely on the mainstream economists since they provide many resources that are relevant in development of the Austrian theories. On the other hand, mainstream economists also need the Austrian economists. Despite the models that they offer, it is meaningful to assume that they are perfect descriptions of the real world. They should put so much faith in these economic models rather should borrow from the Austrian way of challenging the existing models. In closing, urgent review of the Austrian economic theories is necessary by all economists (including mainstream economists) in attaining sound economic systems.

Suggestions for Further Research

Further studies should be done on the Austrian economics; particularly on what exactly is the efficiency of the Austrian economics in handling the financial crisis. Such studies should particularly focus on the practical examples that prove their credibility. Results of such studies could then be incorporated in the mainstream economics especially with regard to stabilizing the crisis.

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