General Aspects of the Economical Crisis

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Abstract: According to the economic theories, crises does not follow a general model, each of them, presenting unique aspects, representing actually an accident, generated by specific factors, at a certain socio-economic and political situation. Like a classification of the crisis we can specify: the crisis of liquidity in the banking sector, external balance of payments crisis, currency crisis, external debt crisis and the financial crisis. After we have analyze the causes of the major crisis in XIX-th and XX-th centuries, we broach the principal causes of the actual world crisis. The implications of the crisis in Est-Europe and in Romania are analyzed from the point of view of these economies vulnerability and a series of mistakes taken in the governance acts. The theory of State intervention in the adjustment of economic mechanisms, due to J.M. Keynes, is bring like an argument for exceed the negative effects of the crisis.

Keywords: crisis; currency; financial; debt

JEL Classification: H12; H63; H68

1. Introduction

Analyzing the evolution of human society it is observed that the economic process in a country of more than one country or even worldwide, pass in certain periods through a State of imbalance, known in the literature as the economic crisis.

Any imbalance of economic activity has adverse effects in the social plan. Under the terms of the phenomenon of globalization, interdependence of international relations, development of transnational companies, crises spreads more quickly from one country to another. As a rule, the contamination of national economies is strongest from developed economies by LDCs.

Fluctuations in economic activity may be seasonal, due to natural factors or social predictable, random fluctuations caused by natural factors or cyclical fluctuations and social unpredictable caused by internal factors and own economic activity which are repeated from time to time, without being able to be placed in a time-accurate, rigorous.

In the literature are known of the four phases of the economic cycle, namely: the phase of recession, depression, stage revival phase and phase economic growth. In the phase of recession there is a decrease in economic indicators (GDP and other indicators) in a given period, to a different reference period.

At the level of economic depression, maintaining low and this phase lasts until the level indicators analyzed begins to increase. Revival phase is characterized by a significant increase of economic indicators and it is maintained until this increase equals the level prior to the outbreak of the crisis. Driving momentum or the end of the crisis starts when there has been a real increase of the economy.

2. The Economic Crisis – Causality and Typology

Economic crisis is a situation in which the economy of a country falls down sharply, generated usually by a financial crisis. In an economy faced with an economic crisis, it is occur, cumulative drop in gross domestic product, a rise or fall down of the prices due to a inflation or deflation. Economic crisis may take the form of a recession or an economic depressions and sometimes may lead to economic collapse.

According to the economic theorists, crises does not follow a general model, each of them, presenting unique aspects, representing actually an accident, generated by specific factors, at a certain socio-economic and political situation.

The complexity of economic and financial crisis has increased depending upon development of capitalist society, the formation of relations of interdependence between the states of the world, reaching a point of maximum complexity in the current economic and financial crisis.

In economic reality, it is not easily to identify when a country enters into a crisis. Most of economists think that an economy step in a recession phase, when after two successive quarters a decrease of GDP took place.

National Bureau of Economic Research (NBER) defines the crisis as "a significant decline in economic activity for a few months reflected in the decline of GDP, decrease in individual incomes, the reduce the level of employment, the decrease of industrial production and consumption".

Crises are considered as events with low probability of occurrence, but they have large implications for society, being at the same time hardly predictable. Considering the crises, over time, were manifested in the most various fields and institutions, the necessity of understanding the mechanisms that generate the outbreak and spread them, caused a deep crisis analysis, making at the same time and a classification of them:

- *The crisis of liquidity in the banking sector* is generated by a shrinking liquidity, i.e., the failure of banks in payment of their obligations in the short term.
- *External balance of payments crisis* defined by Paul Krugman and Maurice Obstfeld is a situation where international reserve of a country falls

massively. Anticipating a depreciation of the exchange rate in the future, banks make use of the purchase of foreign currency operations. Kaminsky and Carmen Reinhart defined external balance of payments crisis being a fall down of international reserves. Assessment of the effects of such a crisis is base on rate of variation of a country's international reserves. The collapse of international reserve does not only happen because of speculation in the currency market but also due to a deficit of current account (in a given time period, imports exceed exports).

- *Currency crisis* is characterized by a significant depreciation of the exchange rate cause by a massive growth of demand for foreign currency. Jeffery Frankel and Andrew appreciate the currency crisis as a situation where the exchange rate is lower for a period of one year, more than 25%, and in the opinion of Gerardo Esquivel and Felipe Larraín currency crisis is manifested when there has been a higher depreciation of more than 10% of the real rate of exchange. Ilan Goldfajn and Poonam Gupta advancing the theory that the currency crisis is an imbalance between the actual and the estimated rate of exchange.
- *External debt crisis*. Rudiger Dornbusch defines for the first time this crisis as a situation in which a country is unable to pay its own external debt. The most important indicators on which it is analysed whether a country is faced with a crisis of the external debt is the amount of external debt in relation to gross domestic product.
- *The financial crisis* is based on a massive loss of investor confidence in the financial system. Because of this lack of credibility, capital are withdrawn from the financial markets and repatriated to their origin country, generating a decrease of liquidity in the stock exchange transactions, a pressure on the exchange rate (on the backdrop of increased demand for foreign currency required for conversion of the amount of money which were not invested any more, on the capital market) and a pressure on interest rates (the reduction in demand for securities).

3. A Brief History of the Economic Crisis

A foray into crisis history shows that no matter how different they were in the past, there is, however, and many common characteristics. The economic crises from yesterday and nowadays, it is considered most of the economists, are generated by a wrong management of a large amount of capital at company level, investment errors of investment having its sources in monetary expansion. Any excess of monetary on the credit market is a fictitious capital injection into the economic system encouraging consumption and indebted and discouraging the savings.

A crisis that had similar causes of the current crisis, by the granting of a large number of loans occurred in 1819 in U.S.A The large number of loans was granted for the purchase of housing, which have never been returned. Keynes and other economists considered the crisis of 1819 as the first financial crisis of U.S.A. which led to the appearance and evolution of the economic cycle.

Another crisis that hit, this time, England, in 1825 spread quickly throughout Europe and in the countries of Latin America, was due, first of all, massive investments in infrastructure, strengthening of the industrial revolution and the costs of war.

At 18 years after the previous crisis, in 1837, U.S.A. repeating the mistakes of the past years, struggled on the background of real estate speculation, with another financial crisis.

Another crisis, considered by many economists first world economic crisis, occurred in 1857, generated by the massive decrease of trade in agricultural products and the bankruptcy of a large number of banks.

On 24 September 1869 was triggered official economic crisis known as "The Black Friday" or the scandal “Fisk/Gould”, determined by the speculative shares with gold.

After a long period of prosperity, through the development of agriculture, in 1873, in the U.S.A. occurred another crisis as a result of speculation and huge costs. Because of panic who was installed and Jay Cooke & Company bank’s bankruptcy, the stock markets have collapsed, and the New York Stock Exchange was closed for 10 days. Unemployment rate climbed to over 14%.

One of the biggest economic shocks in France represented the fall of the stock exchange of Paris in the year 1882. Because of the large requests of credits, as a result of the increase in prices of shares and not to be suspected of lack of funds, the banks have falsified public reports. Being unable to recover the money with proper interest, the banks have failed, stock exchange has closed and thus the crisis broke out, extended over a period of several years.

The financial crisis in 1884 was also determined of the fall of the stock exchange of goods and financial speculation which led to a massive drop in people’s confidence in the banks’ activity.

The crisis which has affected the financial system in the period 1893-1894 is considered by economists one of the most dramatic from the history of stock exchange. In 1894, value of the stocks of the most companies have reached the lowest level of 1878.

In 1907, there was another big financial crisis known as the "Banking Panic of 1907" when the New York stock exchange has lost more than 50% of the value of the goods, this affecting a large number of banks and investment companies.

One of the most interesting subjects from literature is the economic crisis of 1929-1933, which has triggered in the United States of America and it has spread throughout the world. All specialists who were in-depth analysis of the economic impact of 1929, economists, sociologists and historians have not reached an unanimously point of view about causes that have determined it.

The theory of monetarist supporters, including Milton Friedman, considered that the Great Depression was caused by monetary contractions as a result of unhealthy monetary policy carried by the FED, affecting the entire banking system. Another group of economists, taking it as exponent on J.M. Keynes, supporting a structuralize standpoint, giving the explanation for this crisis under consumtion and over investments, while Marxist theory supporters place the origin of the crisis in the sphere of production.

Paul Krugman believes that the Great Depression of 1929 "has shown the lack of regulations and supervisor improperly on financial market." The crisis of 1929, known as the "Black Tuesday" or "The great Fall" was the only one which caused huge damage around the world.

Since the 1980s, the global economy experienced a quickly expansion, mainly, due to the economic development of East Asia countries. Because of the United States' economy was considered a safe place for those who wished to keep the savings, many foreigners have took out the savings in the U.S.A., passing into a guarantor of economic stability. The trade balance of U.S.A. was in deficit (imports were higher than exports) and this situation became worse. For adjusting the deficit, it is resorted to a policy of more permissive financial regulations to encourage exports, expanded during the late 9th decade also in the banking sector. These changes increased reduced the communication between the banks and borrowers.

The actual financial crisis triggered for the first time in the U.S.A. in 2007, being preceded by several crises which affected the world economy. Thus, in 1997, the global economy was devastated by the breakdown of foreign exchange market from Asia, and a year later, a similar crisis in Russia. In 2001, in The U.S.A. occurs the economic chaos caused by the massive development of firms who had centered activity on the Internet, so called crisis "dot-com". Shares of IT companies determined the growth of the stock market between 1998-2000.

In 2008, The United States of America faced the crisis again, after a rapid fall of prices on the estate and credit market, turning quickly into one global, considered by specialists much more devastating than the Great Depression.

Major impact on The U.S.A. economy was creating a favorable legislative framework for housing construction, as well as relaxed financial conditions, which allowed access to credits for a segment of the population with low income. Based on those regulations, more and more banks had provided considerable loans for the purchase of dwellings to the clients who lacked the solvency requirements. Thus, appeared the subprime loans that do not require advance payment of the debtor and having a promotional interest rate, too. Those who borrowed expected themselves an increase in value of properties in the future. When house prices fell, most beneficiaries of real estate loans were unable to pay the rates. At that time, the offer of housing has increased on the real estate, causing dramatic decrease in their prices. Investors in this sector gave up their projects being constrained construction activity.

Liquidity crisis that occurred affected institutions that provide direct loans, savings and credit banks (Washington Mutual was one of the most affected banks by the credit crisis and decline of the housing market in the U.S.A), institutions for financing and guarantee mortgage (The Federal National Mortgage Association and the Federal Home Mortgage Corporation, known as Fannie Mae and Freddie Mac) and investment banks. Losses suffered by those two institutions guarantee mortgage contributed to lower growth rate of the American economy, affecting system credit on the property market confronted with the greatest crisis of the last 25 years. The abundance of credits in competitive conditions, led to a reduction of exigency in lending them, cheaper loans and increasing risk-taking.

With the losses registered by the investors, it was recorded a decrease of shares on stock exchanges and transactions on the real estate market, also. Thus it began the fall in consumption, a reduction in the profit of companies, reducing of the investments, the reduction of operating costs and the increase of unemployment. The financial crisis has evolved into a very fast pace, affecting the world economy in all sectors.

4. The Implications of the Crisis in Est-Europe and in Romania

The year 2009 was one in which, under the influence of external and internal dramatic events, financial and economic crisis rapidly envelops the entire global economy.

On the internationally layout, the gross domestic product was decreased with 0.6%, decreasing that was more pronounced in the United States of America and Europe. In the old continent, the falling of the gross domestic product was more extensive, nearly 4%. Although incentives have been taken by central banks and authorities, the European Union recorded a deficit of about 7% of GDP and public debt increased by 12%.

Eastern Europe was the region most affected by economic crisis. Thus, since 2009, export markets began to fall due to withdrawals of foreign capitals, the International Monetary Fund's involvement was needed to help countries like Hungary, Romania, Latvia, Ukraine and Serbia. Almost two thirds of emergency loans from the IMF globally focused this part of Eastern Europe.

Up towards the end of 2008, the economic growth of Eastern Europe's countries was about 7-8%, which was due to the fact that in the 1990's, countries such Romania, Bulgaria, Hungary or Poland turn to the market economy and to a certain financial stability.

The experts, who have warned yet from 2006 that Eastern Europe will be most severely affected in terms of a future crisis, consider that the countries of this region (Estonia, Latvia, Lithuania, Belarus, Bulgaria, Ukraine) have made a big mistake by setting a fixed exchange rate. The safety of a fixed exchange rate has increased the incentive for the short-term borrow money from banks in Western Europe, which has given rise, increasing the pace of monetary expansion, an increase in inflation since 2006. Ukraine has witnessed the highest rate of inflation which, in May 2008, reached 31%.

Banking systems in Eastern Europe, born in the past two decades, have not yet reached the level of maturity of those in the West, being much more vulnerable in periods of crisis. A rise in bad loans, in the absence of capital injections from the parent institutions, have weakened banks in the region, which led to a crisis of liquidity, affecting the entire European banking system.

In Eastern Europe, the economic crisis was manifested and still manifesting differently depending on the policies of the Government of each country, local conditions and the anti-crisis plan of each State.

Country with the highest economic growth in this region is Poland, whose economy has increased, according to analysts, with 1.4% in the second quarter of 2009.

The economies of Bulgaria and the Czech lands fell by almost 5% in the mid of 2009, compared to the same period of 2008. Gross domestic product of Hungary decreased by 7.4% and of Romania by 8.8% and countries with the most dramatic decreases in Central and Eastern Europe are the Baltic States, which were faced with the dramatic decline of gross domestic product: Estonia - 16,6%,Latvia - 18,2%, Lithuania - 20.4%.

At the end of 2009, Romania's public debt was 23.7% of GDP (lying within the ceiling of 60% of GDP, according to the Treaty of Maastricht). A serious problem is, in this case, the pace of increasing public debt, with approximately 10% in one year.

In Romania, the economic and financial crisis was caused by decrease in export markets of Romanian products, the decreasing of foreign investors confidence on emergency economies, the depreciation of national currency, reducing lines of credit for private foreign parent banks, as well as the increase in loans in assets of banks.

The outperformance credits have increased (according to BNR' Report on the financial stability in 2010) during the period December 2008 to June 2010, from almost 1% to 8.9% for the Bank's portfolio of companies and from 0.8% to 4.5%, respectively for the population sector portfolio.

In 2009, the Romanian economy has fallen by 7,1%, and the fiscal deficit increased considerably. For the first half of the year 2010, financial analysts have forecasted a continuation of economy syncopation with 1,5% from the same quarter of 2009, which it was and happened otherwise.

This decrease was manifested as a result of a lower internal demand and the large number of raw materials and materials which are found in the composition of the Romanian export flows. The volume of investments decreased, too, a decrease of approximately 30% in 2009, keeping going to fall with the same intensity in 2010 also. This negative evolution in the investments takes place as a result of a reduction in profits of firms, decrease access to long-term financing and aggregate demand. Most affected were small and medium enterprises which have had to reduce the most investment.

A situation, also dramatic, has known labor market in Romania, the unemployment rate in June 2010, reaching a threshold of 7.4% (in December 2008, this threshold was 4,4%). The reducing of the number of jobs, as well as dwindling confidence in the safety of the workplace, led to the fall in consumption and the decrease in demand for credit from the population.

5. Conclusions

The phenomenon of crisis is inextricably linked to the economic activity, meaning that, except for the effects, often harsh, in economic, social or political, manifesting itself as a "surgeon" of development, resetting or revaluing the relations or arrangements for production-level territorial or global.

If at first, the economic crises have had more of a local nature (in particular until the Great Depression), with the emphasis on the phenomenon of globalization, they have expanded rapidly in both the area of action and the speed of propagation in time and space. Interlocking becoming more pronounced between the economies of the world have led to the causal chains, but longer and closer.

History of the economic crisis, in the last two centuries, has revealed a few somewhat heterogeneous causes that contributed to the occurrence thereof and, by default, an equally wide variety of ways exceeded them.

At a first glance, it seems at least paradoxical the fact that the majority of the economic crisis was triggered in the U.S. Studying the influence and the implications of American financial capital in most countries of the world, the phenomenon starts to articulate a coherent explanation.

New computers technologies have enabled both a faster scrolling of business and financial transactions, which have been constituted for in a "heel of Achilles" for the world economy.

Any malfunction manifested at the level of one of the influenced factors of the Planet, propagates in a speedy pace by all dependent economies.

The analysis of the crisis in the last century, reveals a certain repeatability of the causes thereof, and may highlight: un-sustaining economic growth, periods of speculative excess or monetary policies of the unhealthy over-estimating massive loans.

Despite some criticism to the theory of Keynes, the State interference in the adjustment of economic mechanisms is becoming more necessary, being already present in the traditional liberal economies such as that of the United States of America.

Sometimes cumbersome, the mechanisms of decisions factors, in particular at political level in some countries, may delay the limitation of the adverse effects of the crisis and the adoption of measures of exceedance, what, from the perspective of globalization, can increase and sometimes worsen, the duration of manifestation of macroeconomic imbalances.

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