

## THE GLOBAL FINANCIAL CRISIS GOES DOWN

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From August 2007 and until the end of 2009, the global financial crisis has broken out in force, at first in the United States of America, with the power of global expansion on long time, and gives also signals of exhaustion by scientific constraints. For the Fed chairman, Ben Bernanke, the thorough knowledge of the offensive factors, the comparisons with the events of 1929's crisis and markets regulations for the beginning, combined with correct evaluation of the phenomenon duration.

Remarkable and numerous financial approaches belong to Nobel laureate J. E. Stiglitz. The latest study reproduced in the newspaper Romania Libera (November 3<sup>rd</sup>, 2009 ) coauthor George Akerlof. The title of the study is significant "new freedom for economical thinking".

From the beginning it is emphasized that the economists have challenged old history ideas, while science is defined by forecasting future. The wealth of economical science ideas sustains that these aren't efficient and stable and both economy and society cannot be described through standard methods of competitive balance.

According to the economic behavior, the market participants act irrationally. In the modern informational economy where markets are competitive, they usually are effective when information is asymmetric (some people know this, some don't).

For a research tradition, with models from "rational expectations" school, markets are not stable and produce price bubbles. The crisis has

revived the need to regulate markets, it boosts alternative research favorable for an analysis of a complex economical system and the search for policies which can prevent the recurrence of recent disaster.

It is important to underline that the economical and social science researchers have experienced models, based on agents with emphasis on the diversity of circumstances, as network models, reconsideration of Hyman Minsky's work in the field of financial crises and models based on guilt with a target on explanation for the dynamics of growth. The author emphasizes in particular the following: "We have a lot to learn from the history of economy. With all the financial innovations announced by trumpets, the current crisis and other crises from the past are very much alike...".

**Paul Krugman, Nobel Laureate** made the following statement: "We managed to avoid a second major crisis, but we will be able to talk about a complete recovery in about two years or more. Economical growth and exports show signs of stabilization". Still, government spending are not sustainable on long term, and unemployment is an obstacle which economies have to overcome. Krugman believes that the world faces a prolonged economic slowdown, as happened in Japan in the 90's. In the past, economies have emerged from the crisis through export trading with countries that had foreign trade surplus.

The economists also take into consideration other solutions, like

revitalization of consumption, investment and the real estate market; but there are few chances to boost the U.S. economy. Krugman considers necessary an urgent restructure of the financial system in order to prevent crisis recovery. Also is chosen the idea to efficiently regulate the banking system and to limit the assumed risks.

During crisis everything must be saved and at the end of any crisis everything should be regulated as a bank.

Citigroup, the largest bank in the world, with 276,000 employees, 200 million customers, with operations in more than one hundred countries, publishes the report of its profit from the last two years with a minus of 18.4 billion U.S. dollars in the first three quarters.

Citigroup is part of larger institutions group, deeply involved in the economy and therefore the authorities considered it too big to be allowed to collapse. Therefore, the company has received last year an aid of 45 billion from the state. In addition, through the deposit guarantee authority, government agreed a support for Citigroup with a value of 300 million U.S. dollars.

The bank has reduced the accounting book value of the mortgage balance with tens of billions of dollars, and face also with his great credit card portfolio. With credit commitments of 1,200 billion in the second quarter and also with 873 billion US dollars in credit cards. In October the bank decided to increase rates of credit card holders by 29.99%. Citigroup status requires more than government support. Taking into consideration the Citigroup associate risk, the Congress is concerned that the United States will never recover the borrowed money.

The process of the banking crisis has not ended. In mid-October 2009 three more banks were closed, increasing the number of bankrupt banks to 123 institutions. Orion Bank was established in Naples and managed 2.7

billion U.S. dollars. Century Bank had activities in Sarasota, Florida and 728 million U.S. dollars assets. The third, Pacific Coast National Bank works in California with assets of 134.4 billion dollars, was taken over by stronger banks.

The action was taken through the Federal Deposit Guarantee Agency. The American government spent in 2008, 2.3 billion U.S. dollars in order to stabilize the banking system. Recently Nouriel Roubini, professor of economics at New York University published an article entitled "A Story about Two American Economies<sup>1</sup>". From the beginning, the author warned that the U.S. has reported in the third quarter of 2009 an increase of 3.5% of GDP, suggesting that it ended the most severe recession since the Great Depression. In fact, among small firms production is declining and growth in the third quarter was actually less than 2% of GDP.

According to an extensive evaluation, unemployment rate reached 10.2% and it is prepared to jump to 17.5% when people have given up looking for full time jobs or part-time jobs. According to the companies data, the loss is about 600 thousand jobs. Studies on households reveal a loss of more than two million jobs.

**In the EU the attack of the global financial crisis has acted later** than in the United States and the EU has provided financial support for troubleshooting. After a short period of time in some EU countries have started, with some differences, global financial crisis which in time expands to all 27 states members. While the structures of the EU committed to reduce the crisis attacking forces were accompanied not only by credit operations for the banks and companies threatened by bankruptcy but also the adoption of specific laws, which require common rules for banks,

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<sup>1</sup> N. Roubini - A Story about Two American Economies, Romania Libera, 24.11.2009.

insurers and occupational pension company from the Community bloc. "The unreasonable Financial markets - said European Commission President - Jose Manuel Barroso – are European and Global. Their supervision should be European and global. Our goal is to protect European taxpayers from a reiteration of events such as those from 2008 autumn, when governments were forced to pump billions of euros to the banks.

For macro and micro economic surveillance, the European Commission organized the European Council of Systemic Risk (ESRB) to monitor the risks in the financial system at the "macro" level, designed to provide alerts and recommendations for the EU Member States in order to avoid crises. For the micro level, European System of Financial Supervisors (ESFS) oversees individual financial institutions and will be composed of the National Surveillance Authority and three supervisory authorities: The European Authority for Banking System, The European Authority for the Insurance and Occupational Pensions and The European Authority for Securities and Markets. These three authorities will not take over the role of advisory committees. The European Council of Systemic Risk will provide recommendations and alerts for the European countries and for the three supervisory authorities. The financial supervisory system will promote the principle of "fiscal responsibility". The commission proposals were approved by the European Council in June.

**European Central Bank** withdraws financial incentives as the officials fear that the inflation could rise. European Central Bank President J. Trichet faced the possibility to reduce incentives for the activities that are not up to date. Measures that threaten price stability were suspended. In July 2008 inflation was 4.1% and in June 2009 fell to 0.1%. In the euro area, economy came out of recession, after the period June-

September 2009 when the economy has increased.

The 16 countries from the euro zone announced in the third quarter a GDP growth of 0.4%. Before, the economy contracted in the second quarter. But the EU as a whole came out of recession with a growth of 0.2% in the same quarter three. Italy and Austria have achieved economic growth quarter to quarter, while in the United Kingdom it didn't overcome the crisis, for them GDP decreased by 0.4% between June to September.

**After that, appeared the problem of the public debt of the European Union** which goes up to 100% of GDP by 2014 in the absence of fiscal discipline (analysis of European Commission). Estimations show rapid deterioration in finance at a Community level. Public debt in the euro area increased to 84% of GDP and next year will reach 88, 2% of GDP. European Committee identified 5 high risk countries: Greece, Ireland, Spain, England and Latvia. The increase is followed for: pensions, public health and large budget deficits. On the frame of fragile growth of the EU economy, fiscal consolidation is postponed to 2011. The heads of the EU finance demand the withdrawal of the financial assistance for the banking system. The EU economy will gradually return to a growth with 0.7% in 2010 and 1.6% in 2011. For 2010 the estimated risk for unemployment rate will increase up to 10.3%.

**At the beginning of December 2009, the European Union entered a new era.** The Swedish Prime Minister, Fredrik Reinfeldt, whose country holds the EU presidency, has the honor of an expected 8 years event, with a remarkable beginning. "Today - says prime minister - is an opening a new era of cooperation within the EU. The Treaty of Lisbon, which came into force, the European Union acquires tools that will face new challenges". Within the next two

years and half the former Belgian prime minister, Herman Van Rompuy will be president of the European Council. The Lisbon Treaty has created another important position, namely the EU High Representative for Foreign Policy and Security. This position was taken over by Catherine Asthose which will be also European commissioner for general affairs in the future European Committee. EU becomes the subject of international law and from this moment it could negotiate as an entity with other countries. EU receives a legal personality and can negotiate with third countries.

The European Parliament will have an important role in the process of adoption for most EU legislation, and will increase the role of national parliaments which will be consulted on the adoption laws.

In Central and Eastern, banks faced a substantial drop in their economies, exacerbated in 2009. Erik Berglof, EBRD chief economist, warns about threats of a severe economic decline. "In terms of economic growth, said Erik Berglof, Central Europe will remain behind other countries in the world ... In the next years this will be the region with the lowest growth rates".

Most severe economic declines were recorded in the Baltic, with a significant decline of minus 15.4% in Estonia.

For this area was recorded an exception: **in Poland**, in the first three quarters of 2009 it was a GDP growth of 3% for first quarter, 1.1% for the second quarter and 2% (forecast) for the third quarter (Source for the five countries is Eurostat). For this period of time, zloty appreciated by 6.4% up to a rate of 4.5 zloty-euro. This country benefits of the most and stable domestic market in the region. The structure for industrial production was minus 1.3%, unemployment 8.2% and a depreciation of national currency of 6.4% .

In the **Czech Republic** this year, according to the source Eurostat was recorded a decline of the economy in the first quarter with 4.3%, in the second quarter with 4.7% and with 4.1% in the third quarter. In the same year, industrial production dropped with 11.9%, unemployment reach 7% and the national currency goes down with 5.5%.

According to forecasts (source Eurostat) **Hungary's** economy will shrink in 2009. The first quarter GDP decline was minus 5.6%. In the second quarter fell to minus 7.2% and in the third quarter goes to minus 8%. In last autumn, Hungary went to the IMF and ask for a help in order to avoid national bankruptcy. Industrial production from this country dropped with 15%, unemployment rose with 9.7% and national currency depreciated with 4.5%.

**In Slovakia** the economic decline was tempered. In the third quarter of the country's GDP fell by 4.9% on the same period. For the previous quarter there was a correction of 5.7% for the first three months of 2009 and 5.5% for July-September. In **Bulgaria**, the Finance Minister said that the hardest times for his country just going in the fourth quarter 2009 and first quarter of 2010. However, according to Eurostat, GDP fell by 3.5% in first quarter 2009, with minus 4.9% in the second quarter and minus 5.8% in the third quarter.

**In Romania the global financial crisis attack** has acted later in the fourth quarter of 2008 and was greeted with surprise. Last year it achieved the best economic results, with growth of 9% of GDP in the third quarter but with a sharp reduction up to 7.1% in the last one. Political time was unfavorable because in December the government was changed, and that time was accompanied by a severe financial crisis. The problems which have to be solved were still unknown. In addition, the state budget from 2008, with high income, was settled with a deficit of billions of euros. The resources owned by the state budget for

2009 meant recession, diminished production and investment and GDP, and rising unemployment. Since the first quarter GDP's drop reached 6.2%. In compensation, the government initiated negotiations with the IMF, setting the terms of credit and assigned a 20 billion euro financing. The value of the credit had several stages. The government was made by two parties and after a while the alliance broke with the confirmation of Parliament. In the second quarter GDP fell more to a minus 8.7%. The individualized Government who remained in power for a while, busy with the procedure for concluding the case, lost the fundamental attributes of power.

This phenomenon took place in a period of time when the IMF was supposed to allocate a credit rate of 1.5 billion euros and according to the credit agreement the Romanian authorities had to pass a set of laws. In the third quarter, the drop of the GDP rose a bit up to a minus 7.1%. Current legal problems will be solved after the election of the President of Romania.

The third part of the financing from the IMF was blocked but the government solved the problem with the local banks. There are ten banks who bought 1.42 billion euro on November 26, from this amount 1.2 billion euro fueled the State Treasury, with an attractive interest rate.

Budget deficit requires financing, this was solved with liquid availabilities held by banks at the NBR, this way was compensated the interruption of the external finance. The large amounts which became available for the banks appeared according to NBR decision. This decision was taken in an extraordinary session to cut the minimum reserve for foreign currency deposits from 30% to 25%.

NBR has released an amount of 1.4 billion euros, transferred to Treasury account in order to finance the deficit.

Total public debt increased from first of January 2009, from 22 billion euro, to 29 billion euro in November.