A COMPARATIVE ANALYSIS OF THE SOLUTIONS REGARDING THE CURRENT GLOBAL CRISIS[1]
O ANALIZĂ COMPARATIVĂ A SOLUŢIILOR PRIVIND CRIZA GLOBALĂ ACTUALĂ

ADINA DORNEAN, VASILE IŞAN
FACULTY OF ECONOMICS AND BUSINESS ADMINISTRATION, "AL. I. CUZA" UNIVERSITY OF IASI

Abstract:
The aim of this paper is to analyze comparatively and critically the solutions adopted on international level by the European Union and also by different countries. In the first part, the paper aims at emphasizing the causes of the global economic and financial crisis and its features, including the contagion effect which manifested. In the second part, we consider the main implications of the global financial turmoil in order to emphasize the serious effects of the crisis. Finally, we analyze the solutions outlined in hard-hit countries in order to limit and counteract its effects, the solutions adopted on international level and also the domestic remedies. For this purpose, we compare the fiscal, monetary and budgetary solutions developed and implemented in countries such as USA, UK, Japan, EU countries and, of course, Romania.

Key Words: *financial crisis, global crisis, sub-prime credit, fiscal packages, monetary policy.*

JEL classification*:* E58, E62, E63, G01, G38.

1. Introduction

The present world financial and economic crisis is considered to be probably the worst that occurred after the great inter-war economic crisis, as a matter of fact from the last 80 years. As Alan Greenspan says, this crisis is different from those that he experienced during his life because „it paralyzed at the same time major aspects both of the banking system and of the securities brokerage system" [9, p. 513]. The Nobel prize laureate George Akerlof and the professor Robert Shiller also subscribe to this opinion and they believe that this recession is different from the others [2, pp. 151-152], being a generalized crisis that involves the economy on the whole and it is caused not only by the reduced demand, but it is also threatened by the credit crisis. Other authors [14] have even elaborated studies regarding the recent crisis that they suggestively entitled "This Time is Different". It represents a reason for debates, meditations, interrogations regarding the causes for the initiation of this crisis, effects and solutions for coming out of recession.

The paper is structured in five sections: in the first section we present a short characterization of the present crisis, emphasizing the peculiarities and the starting factors of the present global financial and economic crisis. In the second section, we concentrate our attention on the main implications of the crisis on the world economy and in particular, on the Romanian one, and then the next section is devoted to the presentation of the national and international solutions for the limiting and counteracting of the effects of the crisis that appeared in the seriously affected countries. Finally, we present the main conclusions that we reached following the performed analysis.

[1] This work is supported by the project "Post-Doctoral Studies in Economics: training program for elite researchers - SPODE" co-funded from the European Social Fund through the Development of Human Resources Operational Programme 2007-2013, contract no. POSDRU/89/1.5/S/61755.

2. Causes of the present global financial and economic crisis

Paul Krugman compares the present crisis with the Great Depression (1929-1933). He has posted on his blog a graph comparing the fall of the manufacturing production from the United States, from its respective mid-1929 and late-2007 peaks [1, p. 2]. As Krugman says, at first, the present recession did not hit industrial production all that hard. But the pace accelerated dramatically during the fall of 2008, so that at this point, the US economy is sort of experiencing half a Great Depression.

Beginning with the spring of 2008, the events took an even more serious turn outside the United States, with even larger falls of the manufacturing production, exports and equity prices in other countries. The crisis started in the US was transmitted internationally through trade flows, capital flows and commodity prices. Therefore, the "Great Credit Crisis" [1, p.1] is just as global.

The opinions regarding the elements that started the crisis differ even among the renowned experts from this area. The causes of the crisis are complex, but without pretending to counterpoint a personal point of view comparable as level, we are trying further on to present the ones that we consider to be mainly guilty of starting the present crisis.

The present crisis that had manifested beginning with the year 2007, originated in the subprime credits, a name that disguised the real estate credits guaranteed with the value of the purchased goods, granted to the American citizens that did not fulfil certain credit worthiness requirements (substandard credits). Those loans were distributed particularly beginning with the year 2000. Transformed through the securitized mechanism into bonds (CDO – *Collateralized Debt Obligation*), they were then transferred to banks and investors all over the world, such as the investors that held participations to the BNP Paribas funds and not only, which explained the expansion of the crisis beyond the borders of the USA. Those bonds guaranteed with debenture portfolios (CDO) were certified by the rating agencies in the AAA class. The real estate bubble exploded when the housing offer exceeded the demand for them, determining the lowering of the prices of the real estates and the credits could not be reimbursed, thus entailing huge losses for the buyers of securities based on subprime credits. In that context, the investors in CDO did not find any more buyers to whom to continue to sell and the market reached the point when "it smashed the rosy ratings" [9, p. 513], questioning the manner of establishing the prices by the CDO-s and other "exotic" financial products such as SIV-s (Structured Investment Vehicle) and ABCP-s (Asset-Backed Commercial Paper). The distrust appeared in the investors' community generating a trust crisis. The trust crisis led to the blocking of the banking system. At its turn, it determined the freezing of the inter-banking market and implicitly, the blocking of the entire credit system. The trust crisis could also involve the population, generating panic and rushing to some banks in order to withdraw cash, to some mutual funds and hedge-funds for redemptions. The trust crisis could turn into a liquidity crisis or even a solvability crisis [6, p. 18].

Thus, among the main factors that stayed at the basis of the initiation of the crisis, we can mention: the limits of the American model of economic growth based on credit and consumption demand; the strong disequilibrium of the financial markets from the USA; the financial innovations and big development of the markets of derivative products; the high yields obtained by the operators from the financial markets. Another factor was the excessive growth of the credit volume that was not accompanied by a parallel growth of the domestic voluntary saving [16, p. 15]: the low level of the interest rate practiced by Fed during 2001-2004 (1% – 2.25%) led to a high growth rate of the credit volume, which fed a speculative advance materialized in the substantial increase of the prices of the capital goods, real estates and the increase of the financial assets' rate (assets' bubble). The increase of the interest rate during 2001-2006 (from 1% to

5.25%) and the expiry of the periods for which the guarantees were granted led to the explosive increase of the volume of the falling due not-reimbursed credits. Also, the correction of the speculative increase of the housing prices added to the fall of the mortgage credit market.

Other authors found only three causes of the credit crisis [2, pp. 154-155]: the collapse of the standard credit manner and the resorting to speculative financing and Ponzi financing, two concepts that Minsky developed in his work and that explained the starting of the present crisis [11, pp. 416-443]; the relation between the capital loss and the degree of indebtedness of the institutions that granted the loans or that generated them – depositary banks, investment banks and financial holding companies; and the use of the already promised credit lines.

Alan Greenspan considered that the main factors that started the crisis were the permissive and fraudulent practices of mortgage lending, lacking judgement securitizing of the credit products and the excessive use of the short term borrowed funds in order to finance the long term assets [9, p. 526].

More simply, the financial crisis started as a result of the credit artificial expansion policy [16, p. 15], allowed by the central banks that offered credits at very low interest rates (even negative in real terms), without them being accompanied by the corresponding savings. In that context, a speculative advance occurred ("irrational exuberance"), that had damaging effects on the real economy and that turned into the economic recession. Under those circumstances, the most obvious starting elements were the increase of the price of raw materials, especially of the oil, the crisis of the subprime mortgages from the USA and finally the bankruptcy of some major banking institutions [16, p. 16].

In conclusion, the collapse of the market for subprime mortgages in the United States is the spark that ignited the crisis, but it is *not* the fundamental cause. At the root of the current crisis stay the global imbalances and the underestimation of risk that lead to excessive leverage in the years *before* the crisis [17, p. 21].

Regarding Romania, it was affected through the contagion effect, given the very high dependence of the public and private sector upon the foreign capitals, to which added the major macroeconomic imbalances (current account deficit, public structural deficit etc.) accumulated by the national economy during the period precursory to the starting of the world financial turbulences.

3. Effects of the present global financial and economic crisis

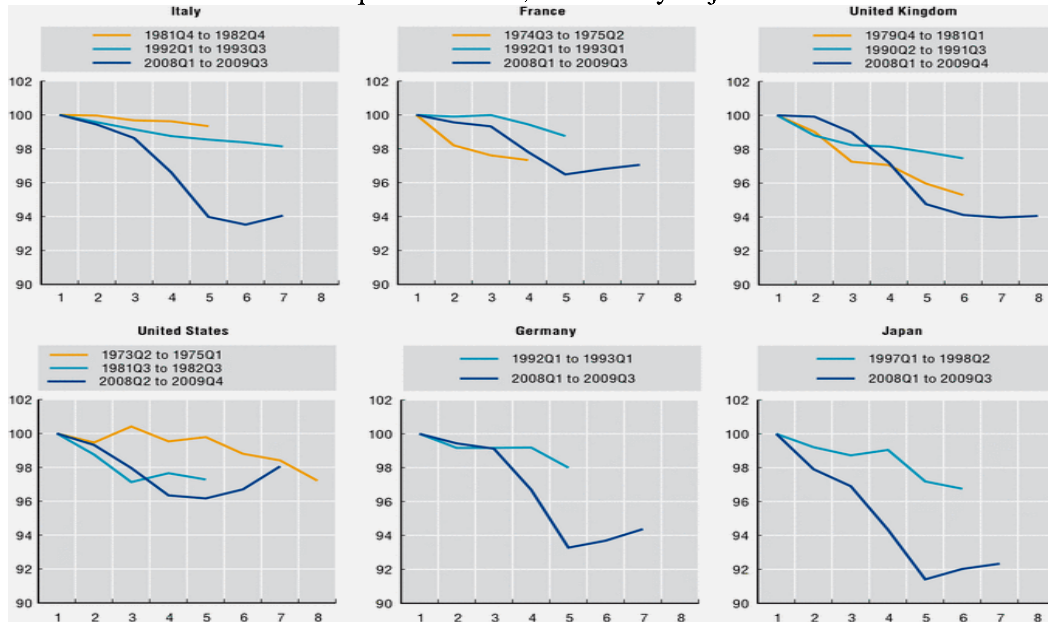
3.1. Global effects

The effects of this financial crisis on the global economy are complex and work across multiple channels [4, p. 2]. First and the most important, the access to bank credit is likely to be highly restrained for a considerable period, as banks seek to reduce leverage and rebuild capital bases. Bank lending standards have already been ramped up sharply, and they are likely to tighten further as weakening economies further magnify bank losses, even while governments are providing public funds to help boost capital bases. Second, access to debt securities markets has tightened dramatically, not just for riskier low-grade borrowers but even for top-rated issuers and short-term securities. Third, the drop in equity prices and residential property values has eroded household net wealth. Fourth, emerging economies are also facing much tighter limits on external financing, as global deleveraging and increasing risk aversion have curtailed investor interest in these markets.

The global economy suffered, so in the forth trimester of 2008 and the first trimester of 2009, it contracted in a rhythm comparable as magnitude and seriousness with the collapse of 1929 and 1931 [15, p. 228]. Thus, although the origin of the crisis was in the USA, the American economy contracted during the two trimesters with an

annual rate of only 6%, unlike Japan that suffered more, its economy contracted with an annual rate of 12.7% in the last trimester of 2008. For most countries, the recent financial crisis led to the sharpest fall in economic activity (measured by GDP) since the Great Depression (Figure 1).

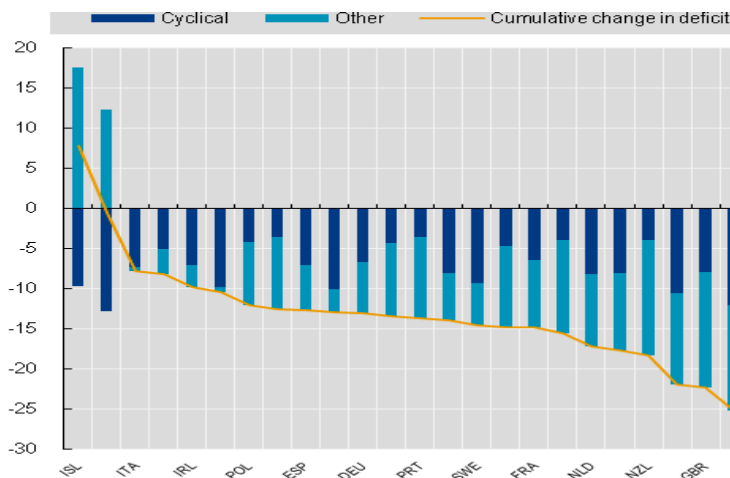
Figure 1 Changes in real GDP of different countries in recent crises
Peak quarter = 100, seasonally adjusted



Source: OECD, *OECD Factbook 2010: Economic, Environmental and Social Statistics*

At the same time, a result of the crisis was a dramatic run-up in government deficits and debt in most countries. The negative effect of the crisis on fiscal positions could be analysed by looking at the changes in general government balances (Figure 2). The decomposition of the cumulative changes into cyclical effects (the effect of the recession in lowering government tax receipts and in raising government outlays) and structural effects (capturing discretionary fiscal policy measures as well as the disappearance of exceptional revenue buoyancy prior to the crisis) was based on the OECD's assessment of the various factors at work.

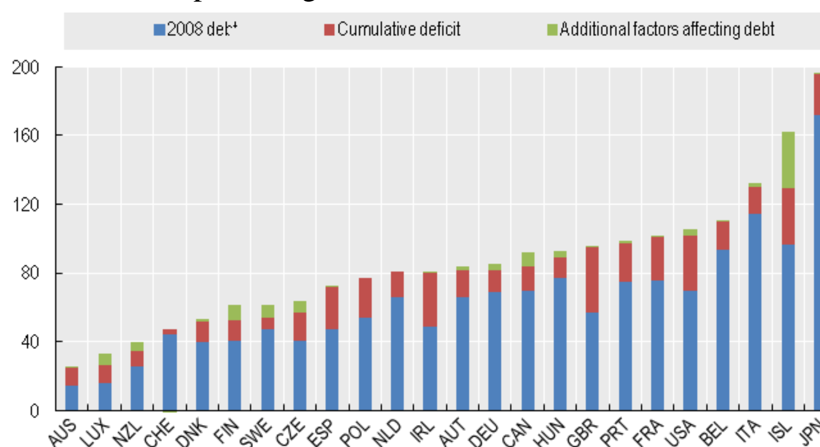
Figure 2 Cumulative changes in government balance, 2009-2011
As a percentage of 2008 GDP



Source: OECD, *OECD Factbook 2010: Economic, Environmental and Social Statistics*

All OECD countries, except Iceland and Hungary, presented large deteriorations in government balances during the three years following 2008. Also, all OECD countries were registering large cyclical deteriorations in their fiscal stance. Structural balances had deteriorated significantly since 2008, with the notable exception of Iceland, Hungary, Italy and the Czech Republic. The deterioration in fiscal deficits was expected to lead to a significant deterioration of public debt by 2011 as compared to 2008 levels (Figure 3). It reflected the impact of both higher cumulative deficits (in most countries) and, to a lesser extent, other financial operations.

Figure 3 Gross government debt
As a percentage of 2008 GDP, 2011 forecasts



Source: OECD, *OECD Factbook 2010: Economic, Environmental and Social Statistics*

The crisis affected countries that were different, such as the mentioned ones, but also Russia, Bulgaria, Croatia, including Romania. The Baltic countries – Latvia, Estonia and Lithuania suffered the most, because the economic contraction was more accentuated in the countries with higher macroeconomic disequilibrium. At the beginning of the crisis, excluding the Baltic countries, Romania registered the biggest macroeconomic disequilibrium than the Baltic countries, but it surpassed the economic contraction as compared to the rest of the countries from the Central and Eastern Europe.

3.2. Impact of the crisis on the Romanian economy

In Romania, although, the impact of the financial crisis on the economy was major, it had mainly manifested indirectly. The transmission of the impact of the crisis was done through five channels: the external commerce channel (as a result of the reduction of the main export markets for the Romanian products); the financial channel (on the background of the reduction of the external private credit lines from the mother-banks, with impact on the evolution of the non-governmental credit); the trust credit (through the increase of the aversion to risk of the foreign investors; the foreign exchange channel (due to the depreciation pressures of the RON) and the wealth and balance effect (at the same time with the substantial reduction of the value of several categories of assets, especially real estates, dominant within the asset class used as banking collateral, as well as through the increase of the ratio of bad loans in the assets of the credit institutions).

Thus, the closer connection of the Romanian economy to the international economic flows (real and capital) favoured during 2000-2008 the catching-up process, but the spreading of the economic-financial crisis from the USA and Europe also affected the Romanian economy, that from a growth of 7.3% of the GDP in 2008 it

found itself in the situation to experience in 2009 a significant decrease of the GDP of 7.1%. At the same time, the budget deficit in 2009 increased from 8.3% of the GDP as compared to 5,4% of the GDP during the previous year [3, 2009, p. 12].

Given the important effects of the global financial crisis, it is necessary to find solution in order to limit and counteract the effects of the present global financial and economic crisis.

4. Solutions of the present global financial and economic crisis

4.1. Solutions on international level for counteracting the effects of the crisis

After the starting of the crisis, the governments and the central banks of the countries affected by the crisis took and applied a series of measures meant to counteract the effects of the crisis and to restore the trust in the financial system. Thus, among the immediate coordinated actions of the governments of the USA and the EU countries, we can mention the support of the banking system through the recapitalization of the banks, the nationalization of some banks, offering governmental guarantees (interbank credit guarantee, deposit guarantee – some countries set up the total deposit guarantee) or toxic asset take over programs, etc. One of the first measures taken by the financial organisms from the USA (Federal Reserve and Treasury) was the application of TARP (Troubled Assets Relief Program), that intended to take over the toxic assets from the "weakened" banks and then to bid them on the free market in order to discover (and at the same time, to validate) their actual price and to create a market for these assets.

At the same time, the cooperation among the main central banks of the world became tighter, so, in order to ensure the financial stability, they elaborated reorganization measures of the financial regulatory and supervisory structure (for example, Blueprint for a modernized financial regulatory structure in the USA or De Larosière Report in UE). In response to the global economic and financial crisis and following the recommendations of the Larosière Group, a new design of financial supervision in the EU was designed through the establishment in 2011 of an European system of financial supervisors (ESFS), consisting of three European Supervisory Authorities – an European Banking Authority, an European Securities and Markets Authority, and an European Insurance and Occupational Pensions. Also, in 2011, a European Systemic Risk Board (ESRB) was established which was in charge of monitoring and issuing recommendations regarding the potential threats to the stability of the European financial system [8, p. 6].

On the Euro zone level, the actions consisted in taking some firm measures for the safeguarding of the common currency, such as the set up in 2010 of the European Financial Stability Facility or the design of the European Financial Stabilization Mechanism (EFSM). At the same time, the conclusions resulted from the crisis of the financial-banking system from the developed countries imposed a rethinking of its functioning and supervision, including through the application of some stricter requirements regarding the capitalization, liquidity and risk management on the level of the credit institutions, such as those stipulated in the Basel Agreement III.

4.2. National solutions

Different countries affected by the present crisis responded differently to it, with notably different monetary and fiscal policies, some more aggressive, others less. In response to the present crisis, most countries adopted broad ranging stimulus programmes, adjusting various taxes and spending programmes simultaneously [12, p. 5]. In the OECD countries, the size of fiscal packages over the period 2008-10 amounted to 3.4% of area-wide 2008 GDP (weighted average) [12, p. 3]. But, the fiscal packages differed across countries not just in size, but also in their composition.

A majority of those countries with "stimulus" fiscal packages (decrease in tax revenues and increase in government spending) gave priority to tax cuts over boosting spending, Australia, Denmark, France, Japan, Mexico, Norway, Poland and Spain being exceptions [5]. The last mentioned countries adopted tightening fiscal packages which consisted in increasing tax revenues and decreasing government spending. In the United States, the balance would shift, with a stimulus entirely focused on tax cuts in 2008 whereas in 2009 about two-thirds would be on spending measures.

Tax cuts were concentrated on personal income taxes in most countries and to a lesser extent on business taxes. Cuts in personal income taxes amounted to 1% of 2008 GDP or more in Australia, Finland, Korea, Luxembourg, New Zealand, Spain, Sweden and the United States. Some countries also cut significantly social security contributions (including Czech Republic, Germany and the Netherlands), while only the United Kingdom lowered consumption taxes by more than 0.5 % of GDP (a generalized but temporary cut in the VAT rate).

On the spending side, virtually all OECD countries launched and/or brought forward public investment programmes. Australia, Canada, Korea, Poland and Mexico were projected to increase public investment close to 1% of 2008 GDP or more. Transfers to households were often made more generous in particular for those on low income. A few countries (including the Czech Republic, Japan, Korea, Mexico, Portugal, the Slovak Republic and Spain) also announced larger subsidies to the business sector.

Also, most countries used monetary policy in response to the crisis to stimulate the aggregate demand. The stimulus from monetary policy took two main forms: conventional cuts in the policy rates regulating access to central banks' credit and unconventional measures for expanding their balances sheets. One important fact stood out as compared to the policy rates of the major central banks: the extremely aggressive rate cuts of the Bank of England and the Fed beginning in late 2008, along with initially less aggressive moves by the ECB.

First, central banks reduced rapidly their policy rates since the onset of the recession. The US Federal Reserve established a target range for its Federal Reserve rate of 0% to 0.25% since December 2008. The Bank of Japan cut policy rates to 0.1%, while the Bank of England lowered its policy rates to 0.5%. The European Central bank cut its main policy rate less aggressively, lowering its rate on the main refinancing operation to 1%. Other OECD and non-OECD countries also substantially eased their policy rates (including Romania).

Second, the unconventional measures to expand the supply of credit generally took the form of provision to banks of greater access to liquidity than would normally be required to keep the market short-term rates in line with policy targets, of expanding money supply through quantitative easing and the creation of excess reserves and of direct interventions in broader segments of the credit markets (beyond the traditional counterparty of banks) that aimed at easing overall credit conditions in the economy.

In Romania, the public authorities had taken tax measures to address the global financial crisis. Beginning with 2009, dividends were exempted from the tax on dividends if distributed and reinvested in the distributing company's own activity, or in the share capital of another Romanian legal entity, for the purpose of securing and creating new jobs. Also starting with 2009, an additional 20% deduction was applicable for qualifying R&D expenses, and accelerated depreciation applied to equipment used for R&D activities. As from January 1, 2009, interest income derived from term deposits and/or other saving instruments was considered to be non-taxable income when derived by individuals. If such individuals were residents in non-EU member states, such income would be exempted from the withholding tax in Romania.

Due to the fact that in 2009, the budget deficit reached the level of 8.3% of GDP, the Romanian government adopted in 2010 a series of fiscal consolidation measures consisting in the temporary reduction by 25% of the salaries from the public sector, the reduction by 15% of the social expenses and the increase of the VAT share by 5 percentage points (from 19% to 24%).

At the same time, among the possible solutions, also stipulated in the document elaborated by the Romanian Government and entitled "Measures for the stimulation of the economic activity", are the improvement of the infrastructure through the rapid absorption of European funds, public-private partnerships and fiscal consolidation that will create fiscal space for the increase of the capital expenses; defining the priorities regarding the public incomes, as it follows: reduction of tax evasion, elimination of exceptions and increase of the basis of taxation, simplification of the tax system, alignment of the asset tax to the European standards (increase of the asset inventory taxes), increase of the non-fiscal incomes; as well as stimulation measures of the private investments by offering benefits or subventions.

5. Conclusions

The year 2012 is still under the auspices of this global financial and economic crisis, although the elaborated and implemented measures, both on international level and on the level of each affected country are considered to be an attempt to solve the problem and to restore the economic growth rhythm. The shock wave started first in the USA has rapidly spread all over the world, as a result of the interconnections between the economies of different states, but nevertheless the impact of the crisis on the economy of each country is different, depending on its peculiarities.

The crisis has determined the adoption of a large number of measures. The possible solutions also differ depending on the manifestations. Thus, for the over-indebted economies, the stabilization and the reduction of the deficits seem to be a priority and for the countries mainly based on exports, it is necessary either an increase of the level of the internal consumption or an adjustment of the production capacities (which will lead to dismissals and increases of the unemployment)

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