
FROM THE WORLD CRISIS TO RECOVERY

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After more than 50 years of economic growth, we are witnessing a world economic crisis generated by a multitude of economic, political, social and other factors. Banks have contributed to the starting of this crisis, especially by making some speculative investments with a high level of risk, as a result of the sub-regulated financial system in which they carry out their activity. It is possible to get out of this crisis by applying a reformation of the way in which the financial sector is regulated and monitored.

Keywords: financial market, economic growth, new regulations, interest rate, reimbursement risk, credit expansion, inflation policy, sub-regulated financial system, monetary excess, monetary relaxation, toxic financial products.

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Banks and their role in the economic growth

After the Second World War and after the settlement of the main issues referring to the world and areas of influence division, we have witnessed, year after year, the global economic growth phenomenon, defined as the ascendant evolution of the macro economical outcome (GIP) or as a country's long-term increase of the global national product and per capita, as an increase of the production capital of a country, identified by the continuous increase of the real national income during several years. Out of the factors that contribute to the economic growth we mention: the material resources, the capital, the technological equipment, the human resources. The global economic growth generates important theoretical questions to economists and arises numerous discussions and questions to governments and enterprises that are invested with the responsibility of coordinating the national components with the purpose of coping with the challenges of the contemporary world.

After more than half a century of economic growth, noticed after the Second World War, we are witnessing a global economic crisis, similar to the one between 1929 and 1933, but different at the same time due to the causes that generated it and to the amplitude of the unbalances it created.

The world economic crisis we are currently witnessing started in 2007 or even earlier and its ending is uncertain due to a multitude of elements which influence it and especially due to the measures which the economic, political and other factors must take in order to surpass it. There is an official explanation of the crisis, provided by public institutions, according to which it originates in the inadequate

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behaviour of economic operators and in the impossibility of the market to function normally, in order to guarantee the appropriate distribution of resources. The economic experts in the field, among whom Daniel Daianu, claim that “*a sub-regulated financial system is at the basis of the current crisis. The deregulation waves in the financial industry brought into the market a lot of appealing products whose risks were superficially understood*”.⁶ In fact, this crisis represents a failure of little or not at all regulated markets and demonstrates once more that the financial market cannot regulate itself. Just as the road traffic needs to set up and observe some rules, so the market economies must be regulated by exact rules that must be observed by all the participants, including by banks, in order for crises to be avoided and potential consequential damage to be limited. The crisis period the whole world has to cope with demonstrates that Keynes’s idea, the great British economist who supported the importance of governments’ intervention to avoid unbalances, is more current than ever.

“Banks are some awesome things when they work properly. And, usually, so it happens. But when it doesn’t, hell on Earth may unleash – so it happened in the United States and in almost all the countries during last year”.⁷

The main error of the monetary policy (Bogdan Glăvan – 2009) is that one regarding a monetary excess, doubled by a process of artificial decrease of the interest rate, these two factors, as well as others, contributing to the unprecedented credit expansion. The factor that generated this crisis is the inflationary policy of the U.S.A, who decided to reduce the interest rate by money issue at the beginning of 2000, with the intended purpose of obtaining a so-called 'monetary relaxation', which was intended to be, at least in statements, the driving force of economic growth.

As a result of this decision, the interest rate decreased from 6.25% at the beginning of 2000 to 1.75 at the end of the same year, reaching a level of 1% in 2003, which was the same until the end of the year. In the same period, Bank of Japan adopted a similar policy, lending money with zero interest at all to the subordinate banks, whereas the Central European Bank reduced the interest rate by almost 2%, keeping it at this level for four years. This way, the interest rate was kept in the euro zone and Japan at a level close to zero. The Central Bank of England was no exception either, keeping the credit interests at a very low level.

The outcome of this policy, which generated economic growth, is represented by the real estate boom that occurred in the USA and the euro zone, as well as in the former socialist countries towards the end of the period. This situation, of investing capital flows in investments with fewer assets and less risky by their nature, such as real estate investments, generated very high profits for investors as long as the market kept on growing. When the subprime panic broke out, the dynamics of deposits ceased to keep up with the evolution of credits, and the banking system accumulated, very rapidly, debts amounting to about 250 billion dollars, most of them at short interest. Great amounts of the money obtained from the Western

⁶ Daniel Daianu , *Capitalismul încotro? Criza economica, mersul ideilor, instituții*, 2009

⁷ Paul Krugman, *Întorcerea economiei declinului și criza din 2008*, 2009

banks under highly advantageous conditions were invested in the developing countries, with very high profits but under risky conditions.

The world capitalist system is under a continuous transformation

In the last decades of the 20th century, major changes occurred in the capitalist society by the occurrence of non-corporeal capitalism, as a result of the technological revolution in the information field. The ideology of the non-corporeal capitalism may be identified in the communication domain and, due to this reason, it allows the cross-nationalization of technologies and communications that move very easily, thus producing globalization. In this situation, brand values became very important, that is why at the end of the last century, the total value of the first ten world brands exceeded, according to statistics, 392 billion dollars, with a clear increasing tendency.

Under the form it developed in the first ten years of the 20th century, this type of capitalism generated major unbalances, especially in the financial field. Thus, in this field, value could be artificially created by means of the so-called toxic financial products, resulted from the fact that banks, in their chase for profit, undertook huge risks by increasing the number of assets that were launched on the market, thus generating major unbalances in their way of operation. To be able to continuously increase profits, banks offered credits without meeting some mandatory conditions, thus contributing to the increase of the risk level, which occurred very often, generating the impossibility of cashing the credits offered and their afferent interests. The phrase “credit only with the ID card”

The major weakness of this type of development, which seemed to generate economic growth, is that it is not sufficiently regulated. The deregulation under Reagan was tacitly accepted as a method to avoid a crisis at the beginning of the non-corporeal capitalism. When non-corporeal assets purchased in the daily basket exceeded the value of the corporeal assets acquired and in order to avoid a crisis there was required the stimulation of some industries that employed many people who, otherwise, could have been unemployed, as well as the identification of some new fields of activity. Out of these industries, the construction and the automotive industries were chosen, and the industry of alternative energy was promoted as a new domain. The construction industry was stimulated by means of the easy access to crediting and by encouraging purchasing 2-3 estates that should guarantee and support each other through the incomes from rentals by their owners. The automotive industry was stimulated by facilitating the access to credits, by stimulating the development of new types of car with special design, displacement, level of pollution, as well as by renewal programs of the rolling stock. The industry of alternative energies was stimulated by means of special advertising that drew attention upon the depletion of oil and gas reserves, as well as upon the danger of global warming, generated by the use, on a large scale, of hydrocarbons. In order to sort out these issues, the programs regarding the alternative energy were encouraged by easier crediting.

All these factors that contributed to the unprecedented development of credit

demand generated the exceeding of certain thresholds, a situation that could raise some questions for banks and governors if they had been granted the appropriate attention. Out of these we mention:

- A longer crediting period than the active period for credit requirement;
- A longer crediting period than the redemption period for the asset purchased on credit;
- The person who received a credit ceases to be employed and becomes a pensioner;
- The share of non-corporeal assets higher than the share of the corporeal assets in the capital of the business enterprise.

By exceeding these thresholds, the reimbursement risk of the credits to debtors increased, thus creating major unbalances in the activity of banks, which represents one of the factors that generated the current world financial crisis. To cope with this crisis, it is necessary to rethink new rules and mechanisms for the functioning of economy and consequently of its financing, and not to take useless administrative measures.

In order to surpass this world financial crisis, we must take into consideration the idea that, no matter severe it might be, it cannot last for ever. Consequently, it is necessary that the experts in this field should set up new rules and mechanisms adapted to the particularities of each field of activity and to each country. In support of this assertion there are the actions by means of which the state, as well as other banks, took over a part of the bankrupt banks between 2007 and 2009, without triggering spectacular reactions at the international level. In this situation there were Lehman Brothers Bank, American International Group and others, which were a breath of fresh air required for the attenuation of the outcomes of the crisis. The main objective of the assistance programs given to the banks and economic operators, financially supported by governmental programs and by IMF and other international banks, is that of preventing some collateral outcomes produced by this crisis, such as unemployment, inflation etc.

Taking into consideration the particular aspects of the crisis in each state, according to the characteristics, particularities, level of development etc. of each one, the governmental programs must be coordinated with each other as well as with the programs of other countries or regions, so that they should not block each other. Governments must develop new regulations concerning the monitoring way of the sectors affected by the crisis, which must be supported by means of national programs. Globalization, with all its positive and negative aspects, cannot be ignored any longer, and isolation, nationalism, protectionism etc. must be left aside, as a first step towards surpassing this crisis.

Developing new rules to avoid future financial crises

The current crisis which occurred in the financial markets all over the world demonstrated that it is time to discuss the necessity of a reform of the regulation and

monitoring way of the financial sector in EU. In this respect, the new legislation in this domain will have as its main objective the improvement of the risk management in order to prevent the future recurrence of another financial crisis. In this respect, a commission of a group of experts was set up, under the chairmanship of Jacques de Larosière, whose main purpose is the analysis of the way in which the financial institutions in the EU countries are organised, with a view to achieving the following objectives:

- ensuring prudential strength;
- creating the best conditions for a better functioning of capital markets and a better collaboration among the EU countries as regards the control of the financial stability;
- creating some suitable mechanisms for the fast warning and management of crises, including for the management of cross-border and inter-sector risks;
- improving the cooperation between EU and other important jurisdictions outside it, with a view to ensuring financial stability at global level.

In order to achieve the necessary level of convergence and cooperation as regards EU monitoring, as well as to achieve the stability of the financial system, it is necessary to integrate the monitoring activities, with a view to sorting out the following issues:

1. High interbank exposures

Taking into consideration that, today, interbank exposures are not risk-free, they should be managed with a higher level of prudence. In this respect, the commission put forward the limitation of all interbank exposures to 25% of their own funds or an alternative limit of 150 million euro, taking into consideration the higher of the two levels.

2. Capital demands and risk management for safety positions

The problem of the potential conflicts of interest from the pattern of the type “originate to distribute” should be settled by guaranteeing that the initiators and the sponsors of credit risk transfers retain a part of the subscribed risks. Out of this reason, it is necessary that investors should make sure that initiators and sponsors retain a material part of the risks. As a result of the agreement within EU between the Parliament and the Council concerning the percentage retained from the total value of the sold secured product, the initial proposal calculated in percentage of 5% of the investment total value was taken into consideration again, so that the initiators and sponsors should be effectively obliged to retain a part of the risks. At the same time, the aim is the setting up of a more rigorous and firm securing frame, which should include additional precaution measures, which should contribute to a more responsible subscription and to the avoidance of huge costs by investors and financial institutions.

3. Setting up monitoring boards

With a view to consolidating the efficiency of monitoring the cross-border banking groups, there was decided the setting up of some monitoring boards, whose

purpose is that of offering competent and responsible help to the authorities in the host state that are responsible with monitoring. In connection to this aspect, the deputies in the European Business Commission within EU consider that this measure represents a first step, to be followed by others, towards the setting up of a solid integrated monitoring system. In this respects, the deputies require the European Commission to put forward a legislative proposal that should comprise provisions referring to the strengthening of the EU role regarding the monitoring system of cross-border banking groups.

4. Hardship clause

As a result of the negotiations within EU between the European Parliament and the Council, a hardship clause was introduced, which requires the European Commission to present, before the end of 2009, a legislative proposal that should stipulate an increase of the retention level in the securing process.

Particular aspects of the financial crisis in Romania

Romania, already in recession, because its GIP is decreasing for the second consecutive term, is no exception and is facing now the same financial crisis that blocked the real estate market, generating major unbalances as concerns both the construction activity and the branches connected to it.

In order to unblock dwelling selling, the new political power came up with a program called “The first house”, whose purpose is that of achieving at least three objectives:

1. To facilitate the access of the interested persons to an advantageous credit that should allow them purchase a dwelling (the first house), with an advance payment of 5% of its value;
2. To unfreeze credit activities;
3. To stimulate the economic activities in the construction field, with positive outcomes upon unemployment, inflation etc.

According to the law, the bank shall issue a unilateral crediting proposal, provided that the state gives a guarantee promise of up to 60,000 euro. On purchasing the dwelling, the beneficiary shall get the money to pay it to the builder, and the dwelling turns into a mortgage of level I in favour of the Ministry of Finances. This program resembles very much with some programs used in the USA, during Bush’s administration, which did not have too much success, because it pushed on the prices and deepened the financial crisis, being a helping hand to the groups of interests and less to the low-income families.

The guarantee of mortgages with public money can lead only to moral hazard, as demonstrated by the American crisis. In the USA, this task was incumbent on the companies with federal support Freddie Mac and Fannie Mal, their guarantees being a stimulant for the various real estate leasing companies to continue giving risky mortgage credits on the subprime segment. Between 2004 and 2006, the two companies purchased bonds covered by mortgages in value of 434 billion dollars, thus allowing the crediting extension to sub primers. These guarantees generated

unbalances in the financial activity of the two companies, saved from disaster by the American federal authorities. This phenomenon is reflected in the share quotations of the mentioned companies, which were transacted below one dollar a piece between 2008 and 2009, while the price in the subprime crediting "golden years" was between 55 and 80 USD per title.

The guaranteeing of some credits for families that did not prove solvable on long term, as well as the capacity to save, demonstrated by the absence of the necessary amount of money for the advance payment, represent a risky game with the money of rate payers, generating the use of some fraud methods against the state by means of a clever shuttle between banks, real estate developers and political factors.

The simplest and healthiest option, both for the national economy and for those who need "The new house", would be that of leaving the market regulate itself, without trying to re-ignite the real estate segment by means of suspicious methods that may generate the decrease of prices. In order to help the young, we do not need to look for all kinds of miraculous solutions, but we must let the real estate balloon deflate, so that the price of dwellings should return to bearable levels by decreasing undeserved profits that some would like to obtain and which society is no longer willing to pay. At that moment, for sure, those who will be able to get an income and save some, without waiting for help that may be disadvantageous for all of us, will be able to solve the dwelling issue in a less expensive manner.

Conclusions

The future regulations that may contribute to the recovery of the financial markets and, implicitly, to the decrease of the banks' risk level, must take into account the transparency, capital adequacy, the elimination of conflicts of interest, the introduction of new monitoring systems for the activity of banks. As regards the banking institutions that practise leveraging, that is which carry out operations that exceed by far their own capital, they must fall under the incidence of regulations, in order to stop these practices. In this respect, there must be taken into consideration the recommendations of the Basel II Agreement, according to which the capital must be adequate according to the risk level, so that money for difficult times should be saved.

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