American Depression Impact on Economical Relations between European Union and United States of America

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Abstract
The world economic crisis is a system crisis that has deep implications on country groups. For the developed countries the crisis means the diminishing of the economic increase rhythm, reduction of new work places creation, unemployment increase, deepening of social tensions and a diminishing of the work productivity increase. Moreover there can be noticed a sustained pressure over the social assistance and protection, over the living level increase and of the antisocial phenomena increase. On the other hand there is a counter-pressure form these countries to maintain certain advantages they have due to the integration policies, advantages that were brought about by the international work division, by the international economic relations based on the comparative cost theory, intensification of armament production and of technical progress of the world finances.

Keywords: economic crisis, financial crisis, price, stock market, capital fluxes, recession

1. Introduction
The financial crisis term applies to some situations in which certain institutions or financial products lose suddenly a significant part of their value. The current crisis, called the “subprime” crisis is considered a financial crisis brought about by the sudden decrease of liquidities on the credit global markets and in banking systems as well, triggered by the companies’ failure that invested in subprime mortgages (that have a high degree of risk).

The crisis causes could have been foreseen even at the end of the last century but the peak was reached in 2007 and 2008. The crisis revealed serious deficiencies in the world financial system and within the regulation frame. The core of the crisis is located in the USA that has been facing with stock exchanges collapse, bankruptcy of some important investment banks, crisis on the credit markets (high debits, impossibility of instalments payments), collapse of the real estates market, unemployment increase, and danger of economic recession. It has already been a well-known aspect that the crisis has become international regarding the stock exchange markets, to which in Europe’s case, the credit markets and real estates market are added. The dramatic aspect of the current moment is revealed by the simulated action of reference interest decrease of EU, Great Britain and USA’s central banks and also of the promised level funds. The financial crisis began at the beginning of 2007 in the USA before it has spread to the entire world economy.

2. United States Collapse
The current situation is much more serious than in any other financial crisis that took place after the Second World War. In the USA the current financial crisis has its causes in the changes applied to the bank legislation in 1999 (Glass Steagal Act), in determining the mortgage banks to grant in a certain percentage quota, mortgage credits to low-income families according to the Community Reinvestment Act, as well as to the FED’s (Federal Reserve System) monetary policy of credit
expansion. All these measures were taken over a 10-year interval both under the democrat and the republican administration and brought in a lot of money in the American bank accounts. However certain risks were taken. When the financial crisis reached its peak at the end of september2008, the American administration took immediately measures to prevent the systemic risk in order to avoid the collapse.

Figure 1 – USA economic crisis (S&P500 Index)

Source: The Wall Street Journal (Market Data Centre)

At the end of 2007, the USA houses price increased by almost 130% as compared with 1997, the starting year of the real estates bubble. In 2006, 28% of the houses were bought as investments and 12% as holiday houses, buy in 2007 these percentages were of 22% and 14% (the percentage evolution shows that the speculators began to leave the American real estates market in 2007). It is estimated that 85% of the apartments purchasing were made with investment purpose in Miami, (2000-2076). The trimestrial index S&P/Case-Shiller registered a steady decrease from the second trimester of 2007, within the context in which the banks became increasingly reluctant regarding the credit granting to some high degree risk clients that depended on the earnings brought in by the house increased price to keep their houses. The guarantees recovery of those that became unable to reimbursing their credits has been added to the statistics regarding the unsold houses and contributes to the houses’ decreasing price.

The monthly composi index for 20 metropolitan regions decreased by 0,9% until 195,62 points in September compared with August, which means 4,9% decrease compared with the same period in 2007.

The two-digit annual increase of the real estates products in the USA proved not to be sustained and of course, the price-rent ratio and price-income ratio that registered rapid increases would definitely have a negative impact. The first clear clue that the mirage of the American real estates products was fading off, the crisis of the middle of 2008 on the high level risk mortgage market (generated by the significant rate of unpayments) triggered loses on the entire set of financial products like the securities or debentures guaranteed by increased level mortgages. The subprime mortgage crisis (with high risk level) turned thus into an all-level financial crisis, which at tits turn, brought about the stock market collapse.

35 S&P500 is the index with the greates cover of the shares quoted on the Wall Street Stock Exchange, reflectaing approximately 75% of the USA economy.
36 http://online.wsj.com/mdc/public/page/marketsdata.html;
The collapse of the real estate market prices between 2007-08 and the more recent losses underwent by the stock markets brought about to the American owners of real estate goods capital losses of trillions of dollars - with an amount estimated at 2,4 trillion dollars in only 9 months until June 2008 (statistics provided by the Federal Reserve, quoted in the World Bank Previsions), and bigger losses due to the recent fall of the stock exchanges. Such big losses will probably have significant impacts upon the consumers’ wealth.

Another aspect, maybe even more important is that many households will be determined by the inability to take out mortgage guaranteed loans. This aspect will have as a consequence the consumption diminishing and a savings increase, on the extent that the households will adjust to the new conditions. The American real estates owners will no longer rely on the price rapid increase that would allow them to purchase new smaller houses after their retirement and to live on their capital earnings. Instead they will have to be more precautious regarding the consumption and to economize a greater part of their current income.

A similar dynamics might be identified in other countries that had even greater price discrepancies in the real estate sector than America at the end of 2007 - like Great Britain and France as well as a series of small economies (International Monetary Fund 2008). The massive price decreases of these markets might have negative effects upon the world wealth.

The probable effects upon the developing countries will be the following: a substantial reduction of their exports, on the extent that the rapid rhythm of the commercial expansion registered in this decade will reduce drastically. International Monetary Fund has recently made the prevision according to which the commercial transaction volume on the world level will increase only by 4,1% increase in 2009, decreasing from 9,3% registered in 2007. An export volume increase has been estimated to register a greater decrease in the case of advanced economies than for the developing economies.
Nevertheless the developing economies might be more affected by the decline regarding the commerce – especially in the case of commodities exports, taking into account the estimated 5% decrease of the price of commodities, other than the petrol ones in 2009. The crisis will have a major negative effect on the investments on the emergent markets. All main external sources of investment funds are expected to drastically decrease during the first wave of effects. Long-term investments will also decrease since the fear of greater risks determines the capital maintaining on internal markets. The global slow down will reduce the commodities and industrial products demand, cutting down export earnings and on the extent that the labour markets will diminish, the abroad workers will probably be affected by the disproportioned impact upon their income which will cut down remittances.

Almost half of the developing countries began to record current account deficits of over 5% of GDP and in some cases the deficits are estimated around 10%. These economies will be very vulnerable to the fluctuations of these external financing sources.
3. Crisis in Europe

Although this generalized crisis initially affected the United States of America, they were not the only ones affected by the negative effects and consumer trust collapse. Many countries which are both developed markets and emergent ones registered unrealistic increases on the assets markets. The financial integration and the trans-national holdings of mutual funds, speculative funds, branches of some developed countries banks and insurance companies have continued the perturbations and have contributed to the spreading of the asset price collapse in the EU countries and in other countries. The international financial crisis has had a negative impact especially upon the American stock exchanges and economies but also upon the European ones and on those from South-Eastern Asia. The snowball effect has been made present all over the world whereas Japan invested 19 billion euros on the market, in Europe, governments nationalize bank after bank.

The leaders of the 27 EU member countries were not indifferent to the crisis effects and to their diminishing. The European Commission presented a plan destined to ensure the EU straightening and getting out of the current economic crisis. The particular plan relies on two main mutual supporting elements. First of all it focuses on short-term measures for stimulating demand, work place motivation and trust re-establishing. Second of all it focuses on the accomplishment and promotion of investments to determine a more significant increase and a long-term lasting prosperity. In order to do so, the plan stipulates the granting of a proper fiscal incentive of 200 billion euros, which is specific and temporary and which represents 1,5% of EU’s GDP. The member countries governments will contribute with 170 billion euros whereas the rest of 30 billion euros will come from the EU budget and from the European Bank.

The straightening plan will consolidate and accelerate the reforms started within the Lisbon Strategy for economic and work places increase. This plan includes concrete and extensive actions on the national and community level, of supporting the agricultural farms, industry as well as of channelling the state financial support towards the most vulnerable categories of the national economies. The official statement of the European Commission is that in the „euro zone” has been officially declared recession, after consecutive decreases of 0,2% over the last three trimesters. The EU commission states that the adopted plan will not affect the 3% ceiling of budgetary deficit set in the Stability Pact. However, Germany and France show that the effort of economic crisis abolition require more flexible conditions regarding the government indebtedness. The main priority is to protect the European citizens against the financial crisis negative effects, in this category being included the employees, households and entrepreneurs. The commission suggests the simplification of the fundamental criteria on which financial assistance is granted from the European Social Fund. Moreover an expenses re-schedule and anticipate payment intensification even beginning with 2009 has also been suggested.

In order to stimulate the work force demand, the Commission invites the member states to take into consideration the diminishing of the social security costs paid by employers for the low-income people. The Council aims at adopting he suggested measures regarding the permanent reduction of the VAT quotas for the services that require intensive use of work force. „Intelligent investments” is a chapter of the straitening plan, namely investments in education, formation and training that would allow citizens to protect their work places and to come back on the labour market to the newly created work places, thus contributing to the work productivity increasing.

The straightening plan will provide supplementary support to the infrastructure investments and energetic efficiency, to the environment protection measures and installations, to SMEs including by eliminating the micro companies imposed obligation of drawing up annual accounts, it will also facilitate the participation to the public purchasing contracts and insurance of the invoice payment within one month by the public authorities. There should be a maximum flexibility in applying the norms regarding the state aids, at the same time maintaining all the equality conditions on the market – the suggested fiscal incentive has the role of guaranteeing the state members participation, avoiding a unique approach which may not work due to the ember states different
starting points. The fiscal incentive level is balanced if it is stipulated for a limited period of time, after which each state member should get back the budgetary deficit – ambitious structural reforms that are stipulated in order to accelerate and consolidate the recovery and/or avoid a future crisis. Some of these reforms will finish the fiscal incentive to increase demand, by supporting the purchasing power through market working improvement. The structural reforms should consolidate the instruments that guarantee the accomplishments of the commitments that were taken on within the Lisbon Strategy for the economic and work places increase.

The authorities continue to mobilize themselves to support the banks. In Belgium, the government announced that it guarantees with up to 240 billion euros the loans that had been taken out by the Fortiz and Dexia Banks. The parliament from Portugal approved the amount of 4 billion euros suggested by the government to support the local banks to improve their capital level within the financial crisis context.

The government will take over temporarily the preferential shares within banks in exchange for financial support. The analysts are estimating that the Portuguese banks will survive the financial crisis due to the strict conditions of the credit granting and also to the fact that there has been no real estates boom over the last few years. France announced that it will also guarantee loans that work out at 55 billion dollars and Luxemburg will provide other 5 billion euros. Belgium and Holland have been carefully monitoring gigantic companies like ING and KBC. Ireland has taken some courageous measures of guaranteeing all the population deposits for 2 years time.

Spain, Ireland and Great Britain will be the most affected countries by the economic problems within the next period of time. This aspect is mainly due to the fact that their economies depend on a great extent on the construction and financial sector. The unemployment increase will have a negative impact upon the consumption and economic increase in general.

The Hungarian banks will have access to a sector support that amounts to 600 billion forints (2.3 billion euros) form the 20 billion euros credit line made available by the International Monetary Fund, EU and the World Bank. The amount of 600 billion forints available for the Hungarian banks of systemic importance will be used to increase the banks capital rate up to 14% and for a interbanking loans guarantee fund. The Hungary government is looking for reaching a consensus with the commercial banks to diminish the risks of the real estates loans granted in foreign currency and to create a working out strategy of the private debt issue. The Fund has also greenlighted a 2.1 billion dollars loan for Island, as part of a total financial support of 6 billion dollars that would be provided together with other countries (Poland offered 200 million dollars) under circumstances in which the island economy has been significantly affected by the credit crisis. The euro zone economy that has registered increases in every year since the group as set up in 1999, compressed by 0.2% in the third trimester of 2008. The euro zone’s annual inflation is currently of 3.2% more above the established target by BCE of 2% but the economists are estimated a significant slow down over the next few years.

Conclusions
Methods of surpassing the economic crisis
In order to diminish the financial crisis consequences, the influence reduction on its real sector, not allowing its transformation into one of economic proportions, the USA financial authorities and then those of the EU, Japan, South Correa, Australia, Canada, China, etc., have been takes a series of solid measures. Among these measures there should be mentioned at least the following ones:

a) setting up of public and public-private funds to support certain financial institutions that are encountering difficulties, by purchasing their shares. For instance, to the USA Treasury’s suggestion (Minister of Finances) was urgently adopted (October 2008) the Law of Economic

37Diego Iscaro analistul Global Insight;
Stability. The above mentioned document allows the treasury to buy back the „toxic assets” of the important financial institutions but being on the verge of bankruptcy. Thus a 700 billion USA dollars fund was set up. For instance it started the compensation process of the securities of two giant USA companies of mortgage re-financing namely Fannie Mae și Freddie Mac. For each of these companies were estimated 100 billion dollars.

b) the governments of some particular countries virtually triggered some etatization processes (partially, major or integral) of many important institutions. For example, Great Britain considered as Europe’s financial centre has partially nationalized 8 of its banks by purchasing their „toxic” shares: Abbey, Barclays, HBOS, HSBC, Lloyds TSB, Nationwide Building Society, Royal Bank of Scotland, Standard Chartered. The government used 50 billion pounds (65 billion euros or 87,5 billion dollars) . In this context some countries authorities’ intentions to privatize different economic entities are rather vague. Under the crisis circumstances the role of the state in economy should increase.

c) to avoid/diminish panic as well as to with draw bank deposits, in most developed countries have been substantially increased the ceilings of the guaranteed amounts of money. For instance in the USA this indicator was increased from 100,0 thousands dollars (which insured over 98% of the deposits) up to 250,0 thousands. Virtually it means that the bank deposits are almost entirely guaranteed. Similar decisions have been adopted by the EU countries. Most EU countries agreed in October 2008 to raise the guaranteed deposits ceiling from a minimum of 20,0 thousands euros to at least 50,0 thousands euros. If we take into account that in more states the „old minimum” covered more than the 9/10 of the bank deposits total, then we may conclude that a new guarantee limit insure almost the entire amount of money kept in banks. For example in Romania the old ceiling (of 20,0 thousands), according to the Guarantee Fund of Deposits in Bank Institutions covered 99,2% of the unprecedented sold of the total amount of deposits. In Great Britain it was of – 50,0 thousands pounds, in Italy– 103,0 thousands euros etc. In November similar measures were adopted in Switzerland, Austria etc. The ceiling increase and inter-state deficiency reduction have a positive impact upon the diminishing/exclusion of the money migration due to deposits.

d) Another anti-crisis measure is the merging of different economic and financial structures. The economic and financial increase of the new entities contributes favourably to the consolidation of their resistance capacity under circumstances of instability.

e) An efficient anti-crisis measure represents the diminishing of the interest rates of monetary policy in the fundamental countries and the contribution to the investments increase. For example, Fed has decided in several times the reduction (almost weekly) of the respective rate which reached the level of 1% (at the beginning of November). Similar decisions were taken by the European Central Bank, Bank of Japan, Bank of Canada, Bank of Australia, etc.

Obviously the measures that have been taken require enormous public and private funds. Besides the public (internal) debt increase, the budgetary deficit has also increased significantly. The crisis will pass, but still bear its consequences. Important is to succeed in the future avoid mistakes in economic policies and better coordination at international level. Because the crisis is and will be global.

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