

THE CURRENT ECONOMIC CRISIS REFLECTED IN MEDIA

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Abstract: *This paper deals – in its former part – with three concepts: speculative bull, stock market crash and stock market correction. As a rule, the bulls are considered to be the cause and the stock market crashes the effect of the bulls. In Romania, the financial crisis is the consequence of the overrated consume generate by credits. As any other thing generated by credits, consume must be paid as well. Unfortunately, the payment must be done in the conditions of the international crisis, so it will cost more. The payment deadline is an inevitable thing, anyhow.*

Key words: *speculative bull, crash, stock market correction, leverage, 'Ninja' loans.*

1. Introduction

The financial crisis is a phenomenon of long-time interest for the author of this article, because the market economy holds within itself this specific mode of manifestation which is the stock market crash. This has been the subject of the following articles, published between 2002 and 2005: 'The Financial Crisis in Asia', 'The Crisis of the American Securities', 'The Stock Market Crash from the 19 October 1987', 'Famous Speculators'.

2. From Bull Market to Crash

The bull market is considered a temporary period when, on the economic market, a span of time of extensive demand is followed by an unfounded raise of the prices. Sensing a rising trend on the market, the investors place high pressure on buying, in order to participate to the profitability of the market. As a rule, these

bulls are followed by even faster selling when the prices start to fall.

The economic theory says that the value of an asset is equal to the sum of the actualized current and future gains. We call this value "the fundamental value". Or, we can often find that the market value of an asset is constantly moving away from this fundamental value: we qualify a phenomenon of this type as a "bull market". And yet, its existence, as a rule, is provisory: it ends with a brutal and unpredictable crash of the market prices, which brings the value of the asset to its fundamental level. (Jessua, Labrousse, Vitry, Gaumont, 2006, p.76).

Generally, bull markets develop quite slow, reaching the higher point gradually, during several years. The traders on the market continue to buy, despite of the fact that they are able, at some point, to perceive that the growth of the stocks is false, as it is not based on a firm economic ground. The reason: the allurements of

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instant profit is much stronger than logic. After the bull market has reached its peak, the prices start dropping, and the panicked investors exert massive pressure on selling, which causes the prices to drop steeply. In what concerns the stock exchange, the financial analysts consider that there is a bull situation when the influence of the stock exchange over the economy is higher than the influence of the economy over the stock exchange. This can be considered a common characteristic of all the bulls in the history.

The bull market is an investment phenomenon which proves the fragility of investors' psychology. The investors build their hopes up on the stock exchange so much that they overlook any rational reflection on the present value of the respective assets. Since the bulls have no substance, they dissipate at some point, and the money invested in these actions are blown in the wind.

As a rule, the bull markets are considered to be the cause, and the stock market crashes – the effect of the bulls. A stock market crash represents a significant drop of the global value of the market, attributed to the crack of the bull market. What happens in this kind of situation is that the investors are trying to leave the market, and they have registered, meanwhile, massive loss. In the attempt to avoid even greater loss, the investors try to transmit their assets to the other investors. The panic resulted from this situation contributes to the fall of the stock market, which finally crashes, affecting everybody. Usually, the speculative crashes have been followed by economic depression.

The crash is an acute form of manifestation of the economic crisis and the symptoms are the lack of credit and payment liquidities, the crash of the stock market and credit instruments, the underestimation of the national currencies. Following the crash, a sudden chaos occurs

in the economic life and bankruptcies multiply. Typically, the crash starts at the stock exchange by a strong drop of the stock trend. (Marin, Puiu, 1993, p. 214).

It is important to distinguish between the terms of stock crash and stock correction. The stock correction can be seen as the method by which the market slows down the over-enthusiastic investors. Generally, a stock correction should not create a loss which could be higher than 20% of the value of the market. A correction does not reach its full purpose unless the steep downward trend stops within a reasonable period of time.

3. The Present Financial Crash

The invention of the derived financial instruments has allowed the reaches to multiply by a range between 25 and 40. A dollar has created other 40 dollars overnight, hidden within sophisticated financial instruments, then sold all over the world, as mutual investment funds, retirement benefit plans, bank accounts. It has been both a greedy and corrupted sale, but legally covered by the lawyers and rating agencies. It was the American bankers as well who realized that what they had created and sold everywhere could no longer be controlled and they decided to reverse the process. What is happening now, simultaneously with the stock market crash, is the absorption of the artificially created riches. The difference from one dollar to 40 which can be found in the price of the shares, of the houses, of petrol, of luxury disappears. The products all stay, but have a different price. Those who have been caught in the middle are carried away by the reflux. In fact their assets are being nationalized by means of the most transparent, pure capitalist instruments. The state intervenes not in order to save the shareholders, as they have lost long ago, but to warrant the debts of

the companies. If it wasn't for this intervention, the crash would have transformed itself into a chain reaction. But the problem is paying the debt, not the shareholders' money. Why did the state intervene to save the system? Because everybody thrusts the state, believes that the state cannot become bankrupted it will honour its obligations. What will follow? We will certainly be poorer, because the nationalization of the assets will affect everybody. Nobody can escape. The question is where, when and how will the new riches be created. How will it look like? (Hostiuc, Business Magazine, 206/2008, p.12) What is interesting is the fact that the liberals, who pretend that the state should retire from the economic life, are the first who demand the state's intervention in the economy in times of economic crisis, precisely in order to save the system.

3.1. The Financial Crisis in the USA

The international crisis started in the USA, and this was not fortuitous, as this is the place where the financial speculation is at its best. Among the currency transfers, with merchandise and derivative instruments, only 5% are still intermediating real credit transactions, merchandise acquisitions or import-export operations. The rest of 95% is pure speculation, selling and buying of money for itself; currency and interest speculations. And if 95% is as such, it is obvious that the bull market is at any time likely to collapse. The problem is that, during the present capitalism, the bull collapses more and more often and more and more profoundly. It has already happened three times in this decade. The first was the explosion of the soap bubble from the IT industry, between 2000 and 2001, when Microsoft (and not them alone) lost two thirds of the value of their

shares. In fact nobody lost anything, only the market status suffered a correction, and only the speculative bubble was lost. The second collapse was that of the big Enron conglomerate, this time a crisis inside companies. Finally, we undergo a crisis which started in real estate, but has extended throughout the entire market. Real estate loans, which are in fact the cause of the present financial crisis, were granted, beyond any control, due to the greediness of the bankers. Those who took loans to buy houses were not qualified to get them, because they did not present any guarantee! They were not eligible, because they did not have proper incomes, jobs with short term employment contracts, some of them did not even have a job. That is why this type of credits were called 'Ninja' loans (No Insurance, No Job, No Job, No Insurance). In brief, what was put to work here was the banker's greed and the populism of the politicians craving for votes. This made it possible even for homeless people to take sub prime loans (meaning with no guarantee) for houses, even if the fact that the system will collapse some day was not entirely unknown. The mortgage speculations followed. The banks sold the mortgages to some trust funds for half price. The funds, in their turn, sold them further to other speculators. The debtor ended by being fed on by a chain of about seven creditors, and, when he was no longer able to pay, the whole chain was broken. The chain was forged on the idea that the prices are rising. But in the end they dropped, and everybody lost. The wheel turned. There was a mass contamination. Two million two hundred keys were handed on by the beneficiaries of the respective funds. That's how the bull collapsed. The banks had spent their money, by giving loans, and they found their safes empty. That is why they received the help of the American Government. They were, in fact,

nationalized. (Şerbănescu, Formula AS, nr 849, 2008, p.3)

And, since this discussion has reached the point of the real estate lending, here are a few figures: the debt of the estate owners has increased from 680 billion \$ in 1974 to 14000 billion at present. The total debt doubled only in the last seven years. An average family has 13 credit cards, and 40% of them have a balance brought forward credit in rising as opposed to the 7% from 1970.

The governments can nationalize companies, can prescribe vacations for banks, can suspend the transactions for weeks, can buy debts or shares and can renegotiate mortgages. The most important thing is that the American Government can issue banknotes. All these instruments have long term effects which are extremely grave, but this means nothing when compared with the collapse of the financial system. The question which arises is: how did it get here?

Even from the '80s, the Americans have consumed more than they produced and they covered the difference taking loans. Two decades of easy money and innovative financial products meant that practically anybody could borrow any sum of money for anything. If the Americans wanted a bigger house, a hi-tech TV or a faster car and had no money to pay for them, there wasn't any problem, they could just take a credit card and they could refund their mortgage and financed all their fantasies. Once the fantasies grew bigger, the same happened with the duty of the estate owners. But the behavior of the regular American was virtuous compared to that of the Government and local authorities. Each and every city, county or state wanted to maintain their many and prosperous operations without increasing the taxes. What is the exit from this vicious circle? It is by loans, making use of more and more sophisticated financial

instruments. The revenue bonds were based on the footing of the future revenues from taxes or lottery. (These bonds warranted the future federation funding for highways, housing and other objectives.)

The local politicians were not the only problem. Under the leadership of Alan Greenspan, the Federal Reserve had obstinately refused to cause any suffering. Were there problems in Russia? The interest was decreased. NASDAQ had crashed? The interest was decreased. The economy slowed down after the terrorist attacks from 2001? The interest was decreased. Regardless of the problem, the solution was to maintain the cash flow and to impel the economy.

The solution for all the problems was taking out loans. In 1990, the national debt of the USA was of 3000 billion dollars. Until 2000, it nearly doubled, reaching the sum of 5750 billion dollars. In September 2008, the figures increased around about 11000 billion.

If there's a lesson to be learned from this crisis, then it is the old plain economic rule which says that nothing is for free. If we want something, we have to pay for it. Debt is not a bad thing. Used responsibly, it is the heart of the modern capitalism. But hiding the smorgasbord of duties behind complex instruments is a way to disguise the costs, an invitation to an irresponsible behaviour.

At a certain point, the magic accounting had to stop. At that point, the consumers had to restrain themselves from using their houses as banks and from spending money they did not actually possess. At some point, the Government had to confront its debt ratio. (Drăguşin, Money Express, 21-27 octombrie 2008, pp. 60-64).

In the USA, the mortgage loans are classified into four main risk categories: A-paper or prime (the most secure), Alt-A, jumbo and sub-prime (the riskiest). The rating agencies have accorded the

sub-prime credits the AAA rating (the least risky). Synthesizing, the crisis manifested as follows: the drop in the real estate prices determined the depreciation of the mortgaged assets below the value of the credit, and the guarantees were no longer able to cover the credits. The banks, even if they foreclose on the mortgages, were no longer able to cover their loss, and the balances highlight important disequilibrium.

3.2. The Financial Crisis in Romania

In less than two months (September-October 2008), the Bucharest Stock Exchange lost more than the capitalization of 30 milliard euro they owned at the beginning of September. The BET index of the most important ten Romanian listed companies decreased with almost 50% of the value listed on the 2nd of September, and only the absence of the stocks of the Transilvania Bank from the market had kept the losses low, and the index of the SIF, BET-FI, crashed 68%. Making a logical assumption, I consider that the BET-FI index fell lower than the BET index because it had previously increased more. Petrom, the biggest company registered at the Stock Exchange came to the value of 2.5 billion euro, less than its privatization value and the SIFs dropped under 100 billion euro, a figure that did not cover the third part of the value of their assets.

It has to be stated that the final description of the stocks which compose the two indexes mentioned above is valid before the registration of the first consistent rising trend of 75-90% (starting with March 2009). 90% is the depreciation rate for the SIFs.

To be able to make a comparison inside the geographic area of Romania, we need the following reference: the WIG 20 index of the Warsaw Stock Exchange kept

plunging off since the beginning of September 2008 with about 43%, the same descending trend was registered by the BUX index of the Budapest Stock Exchange. The Czech Republic and Austria also recorded important losses, the value of their indexes tumbled 48%, respectively 51.5%.

Which were the causes of the Romanian crisis? Ilie Șerbănescu considers that one of the main reasons was the overrated consume generated by the credits. And, as any other thing generated by the credits, the consumption has to be paid for. Unfortunately, this payment needs to be done in the circumstances of the international crisis and it will cost more. The payment is, anyhow, due to be honoured. For five years, Romania has had economic growth from imports solely. It was imports on credits. Then, the foreign capital was the one generating the raising, not the Romanian one. So, the complexity of the situation is given by the specific manifestation of the Romanian crisis on the background of the general crisis, a fact which adds to the bill, no matter how it came. This happens because it is impossible for one to consume more than one produces without an end. We have consumed as such for an equivalent of 14% of the GDP from import of goods and services, foreign products paid with foreign money, namely with credits from the subsidiaries of the foreign banks in Romania. In the food industry only, we have 3 billion euro consumption per year, from import. The Romanian analyst also notices that the Romanian National Bank (BNR) has become a creditor of the banking system, although it did not count in the credit policy of the foreign banks until the moment of the breaking of the crisis. BNR has desperately tried to dwindle the credit which created a distortion of the economy, which is a responsible policy which many over the

ocean didn't carry out. (Şerbănescu, 2008, p.3).

In 2009, more precisely from spring till summer, the stock exchange has picked up, registering a growth of about 30%. The BET-FI index, which dropped the most in 2008, had the best recovery. The indexes rose all of the year of 2009, so that approximately 80% of the losses of 2008 were recovered in 2009.

4. Remedies and Solutions

On the short term, all the solutions to the present crisis require that the Government assumes a larger part of the debt and more obligations.

For the USA, Barack Obama proposed the firm appliance of a program for the following two years, with the total sum of 825 billion dollars, divided in two equal parts, in 2009 and 2010, destined to give a stimulus to the economy. This program adds to the 'Paulson Plan' from the end of 2008, so that the American economy will be injected with 1500 billion dollars. Among the most important components of the 'Obama program' we mention:

- every American earning under 200000 dollar per year receives a tax reduction of 500 dollars, and the families benefit of 1000 dollars reduction;
- other reductions estimated around 275 billion dollars are expected to revive the consumption, which generates two thirds of GDP;
- 119 billion dollars go towards the 50 American states, especially for health and administration expenses;
- the most affected social categories – unemployed, social security – receive 106 billion dollars;
- 90 billion dollars are to be invested in infrastructure, 54 billion in the energetic system, and 16 billion in research. (Măşu, Buneci, Gheorghe, 2009, p. 158).

My opinion is that, the way the banks and other financial institutions receive support (AIG was given funds of over 80 billion dollars to be saved from bankruptcy), the same way the cars industry should be supported. It should abandon the gas as the main fuel and to move towards the pollution-free sources. One solution would be the investment in the alternative energies.

This solution is valid for Romania as well, that is the investment in the building of highways, which would create jobs, and in Aeolian and solar power plants.

The main cause of the crisis is greed. In Romania, the fundamental economic cause is the deepening of the external debt, which means that the export was lower than import. We have started to live the American way, consuming more and more and covering the difference by loans. One of the solutions that could help us get out of the crisis is to buy indigenous products (made in Romania). This could help people to keep their jobs. Another solution would be to reduce the difference between the salaries of those employed in the public sector, which are either very big or very small.

An 'anti-crisis' program of the Boc Government, amounting to 52 billion RON (13 billion euro) has three sections which include 23 measures, from which we mention:

- a) Measures for economic stimulation and growth, evaluated to reach 10,5 billion euro:
 - investments amounting up to 10,2 billion euro (7% of GDP); the domains taken into account are the transport infrastructure and housing;
 - the absorption of the public funds and the establishment of an inter-ministerial group to manage this activity;
 - the application of the warranty funds for Small and Medium Sized Enterprises and Cooperatives (IMM);

- raising the ceiling for the cars program from 3000 to 3800 RON, for cars older than 10 years.

b) Social measures:

- compensation of medication on the B list up to 90% for the retired populations having pensions under 600 RON;
- supplementary support for the unemployed by extending the period of compensation with another 3 months, funding with 50% the professional training for employees and other similar measures.

c) Measures for cash flow stimulation

- setting off the debt of the Central and Local Public Administration to the economic entities;
- compensation of the VAT to be recovered with VAT to be paid;
- capitalization of CEC and Eximbank. (Zăinescu, Jurnalul Național, 2009).

I consider that setting off the debts and the compensation of the VAT are not measurements to relieve the crisis, but rather a debt towards related parties, the first, and a natural proceeding, the second.

Referring to Germany, at the beginning of January 2009, the Government announced the main directions of their economic revival plan, with the cost of 50 billion euro, within a span of two years and continuing a previous plan, of 31 billion euro, adopted at the beginning of 2008.

The investment program involves investing in infrastructure to the sum of 18 billion euro; a decrease of 9 billion euro of the contribution to the social security and the division of the sum between the employer and the employee; a variant of the car renewal program, every buyer being given the sum of 2500 euro to buy a new car on the condition that he brings a car older than 9 years to be quashed; every child will be given once the sum of 100 Euros at birth. In this manner, the German Government takes measures against the crisis with a program of a total value of 81

billion euro, which represents 3,2% of their VAT estimated for 2009-2010. (Mășu, Buneci, Gheorghe, 2009, p.171).

5. Conclusions

The idea of a world conference to debate the need of a world-wide action for a 'capitalism of entrepreneurs' against of a 'capitalism of the speculators' has the president of France, Nicolas Sarkozy among adepts, together with head of states like Great Britain, Germany, Italy and other European leaders. Among the principles of action are the following:

- all the banks will be given support, the European states offering their assistance to the financial institutions having difficulties, each states taking their own measures;
- the managers proven guilty will be made responsible and penalized, with reference to the bank managers which will be asked to resign without hefty compensations as in the USA
- the states are permitted to breach the European ceilings regarding the public debt;
- all those acting on the market will be audited – the rating agencies, those evaluating the risks, the trust funds and the banks will be thoroughly controlled in order to avoid the side-slips. (Mășu, Buneci, Gheorghe, 2009, pp. 166-167).

The initiating group continues to appeal to the restructuring of the world finance by organizing a G-20 summit where, besides the European countries mentioned above should also participate the USA, Japan, China, India and Brazil. Canada, which has a strong banking system, is absent from this list. The growing importance of the countries emerging on the financial arena, especially those from the BRIC group (Brazil, Russia, India and China) has to be underlined.

Apart from the measures against the crisis mentioned above, I believe that other three propositions are also important: the regulation of the activity of the stock exchange, banks and the other financial instruments; the development of a code of conduct for banks and multinational corporations and the development of a trust code for the rating agencies.

In the USA has recently appeared a legislative proposition called 'the Volcker Rule', which stipulates the limitation of the dimensions of the big banks. This proposition no longer allows the proprietary transactions carried out by the big banks on the financial and capital markets and, more than that, it does not allow the banks to invest, completely or partially, funds in risky assets. It also envisages regulations which limit the mergers and consolidations in the banking system. (Gheorghe, Adevărul, 25.01.2010, p. 48).

At the Davos meeting, the most important bankers of the world agreed upon the establishment of a global fund to guarantee and insure the banks against a future crisis. This fund should reach within a few years to the amount of hundred billion euro, in order to cover the costs of possible bankruptcies generated by a possible future crisis. This way, the intervention of the public budgets will no longer be necessary. (Gheorghe, Adevărul, 01.02.2010, p. 48).

About Romania, I consider that the 'First Home' program should be continued with a 'First Silo' for the youth in the countryside and a 'First Business' for the young persons under 30 years of age, with tax deduction for the income tax on condition that at least five jobs are created. The government should definitely invest in infrastructure (which is building highways, water and gas plumbing, railway modernization).

As a conclusion, to emerge from the crisis is, for the involved governments, to assume the responsibility of public expenses able to re-launch the economic 'engine', but only to the extent that connects them to the economic growth.

The economic crashes world-wide are more and more powerful and more and more frequent (we have just seen the third in ten years), which proves that the capitalist system is not based on stable footing.

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