Entrepreneurship
ISSN: 2738-7402
DOI: 10.37708/ep.swu.v11i1.6 *Volume: XI, Issue: 1, Year: 2023, pp. 61-78*

THE ECONOMIC CRISIS AND "THE GREAT RECESSION"

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Received: 25.01.2023, Accepted: 30.03.2023

Abstract

Economic crises are common as instability is an inherent feature of the economic system. The purpose of the following paper is to present the impact the financial crisis in 2008 had on the worldwide markets and economies. A bibliographic review of the subject is presented to provide the reader with more integrated knowledge about the conceptual framework of the economic crisis. Special emphasis is given to the content of the economic crisis, the causal factors that contribute to the outbreak of the economic crises and the effects that they may have, as well as the different types of economic crises to come to the impactful financial crisis in 2008. Finally, an attempt is made to research the origins and the key events that triggered its beginning and spread to the whole world.

Keywords: *economic crisis; economic cycles; financial crisis 2008; causes*

JEL Codes: *E32; E34; G01; G15*

1. Introduction

The idea of a crisis is multifaceted; it denotes the existence of a challenging issue, the occurrence of an anomalous or crucial period, or the occurrence of an anomalous or critical era (Nteka, 2021). Economic crises through the years differ not only in duration, nature, and intensity but in the geographical area they take place and most of all the impact they have. Great attention is given to comprehending and explaining the causes and effects of the crises.

Crises are closely related to financial institutions and banks that are the first to experience any change and imbalance a crisis comes with. However, citizens are those who pay the highest price. History has shown us that the global economy has been devastated by a number of crises, but the worst was the 2008 outbreak, which is comparable to the one that happened back in 1929. However, many economists admit that the financial crisis in 2008 was much more intense and impactful.

It is widely agreed that since the advent of financial crises in 2008, the western capitalist world had already undergone many crises with different intensities and impacts but the recent one is considered the most severe financial crisis, especially compared to the Wall Street crash of 1929. Undoubtedly, it has affected not only

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almost all countries, including the most developed and advanced nations and the weak economies worldwide but also has had adverse effects on individuals' quality of life. Many factors contributed to the emergence of this financial crisis.

This paper examines the theoretical underpinnings of the current financial crisis, paying particular attention to the economic cycle and the phases that make up an economic cycle due to the relationship between them. Moreover, we focus on the financial crisis of 2008–2009 highlighting the key events that triggered the financial panic in September 2008. We discuss the proximate causes of the crisis, including the kinds and the characteristics of the crises in general while we mention the role of more fundamental macroeconomic determinants.

The information mining through the followed methodology and the literature review allows a wide applicable range of scientifically supported views while conducting a systematic review of the current scientific literature.

2. Literature review

The term crisis is used to denote the abnormality, difficulty, and irregularity of a situation during a critical period. According to Panigyrakis crisis is "an abnormal state which is characterized as a critical, difficult, and dangerous situation. Specifically, the crisis is a diversion from a state of regularity and may receive degrees of irregularity from a state of simple disturbance up to the state of uncontrolled explosives events and the state of chaos and panic" (Panigyrakis, 2001).

According to Barton (2004), a crisis is defined as: "a big, sudden event, which is likely to have negative effects. The fact and its consequences can seriously damage an organization and its employees, as well as its products and services, its financial status and reputation".

Additionally, other researchers conclude that "An economic crisis represents a sharp deterioration in a set of economic indicators, an imbalance between money supply and demand, and a fall in asset prices, accompanied by the failures of financial institutions such as banks" (Busuioc-Witowschi, 2010).

Kindleberger and Aliber (2005) raised a rhetorical question as to whether it was possible to predict when a crisis would break out. The answer was given before, that it can be achieved through the process of calculating the continuous decline in profits, which is proven to lead to a crisis.

In a more general treatment of the crisis content, "A financial crisis is perceived as a period during which the market experiences a fully perceived strong downturn of the underlying factor" (Sharpe, 1963).

Referring to the economic crisis, it has been proved that many economic crises were closely related to bank crises since many businesses went bankrupt and closed down. Based on this correlation. Minsky (1972) developed his theory about the economic crisis saying that an economic crisis is characterized by a sharp decline in asset prices, as well as corporate bankruptcies. Moreover, Mishkin supported that

"The financial crisis is a disruption of financial markets, which exacerbates the problems of reverse option and moral hazard, resulting in the inability of financial institutions to channel funds effectively to the most profitable investment opportunities" (Mishkin, 1991).

The level of production, GPD, investments, income, prices, employment, and other macroeconomic variables constitute the economic activity of a country and over time they do not remain stable but they increase or decrease slowly or rapidly. These changes are called **economic cycles** and are characterized by a systematic cyclicality.

The economic cycle, also known as the business cycle, consists of expansion and contraction periods. The present stage of the economic cycle can be determined by variables such as gross domestic product (GDP), interest rates, employment levels, and consumer spending (Estevez, 2019). Understanding the economic cycle can assist investors and businesses in determining when to invest and when to withdraw funds, as each cycle affects equities, bonds, profits, and corporate earnings.

The most commonly used and prevailing concept that better defines the economic or financial crisis is that of the theory of economic fluctuations. According to the theory of economic fluctuations economic crisis is considered one of the two phases of economic fluctuations and specifically the phase of decline, due to the noticeable and permanent decrease in economic activity.

Economic fluctuations are defined as successive fluctuations of economic activity within an economy. They are also called economic cycles or cyclical fluctuations. The British refer to the phenomenon as "business cycles", precisely to emphasize the special importance of investment in the evolution of the economic cycle. Long-term statistical observations have shown that economic cycles last from about 8 to 11 years (European Commission, 2009).

We specifically refer to the phases of a nation's economic activity when we use the terms **economic variations** or **economic cycles**. The terms refer to the expansion and contraction of economic activity, which are marked by persistence, i.e., growth is followed by further growth and fluctuations by other fluctuations.

Economic cycles, on the other hand, are non-periodic, that is, they are not seen at regularly predictable periods and do not persist for a specific amount of time. Economic cycles also range in size and duration and are not cyclical, which means they do not behave consistently and in a predictable manner across all of their manifestations (Knoop, 2004; Howard, 1991). Yet, economic cycles are recurring. As the economy expands from top to bottom or vice versa, it called a complete economic cycle (Burns & Wesley, 1946).

We will also examine the economic cycle to give a more complete picture of the financial crisis. The following clarification regarding the ideas of the economic cycle and the economic crisis is thought to be significant. The many phases that the economy experiences as well as the causes that contribute to these phases are highlighted by economic cycle theories.

The theories of economic crises, on the other hand, focus on the elements that interrupt a specific stage of the business cycle. The economic cycle, which is also known as a business cycle, is the circular movement of an economy as it moves from expansion to contraction and vice versa. Economic expansion is characterized by growth while, on the other hand, a contraction refers to a recession, which involves a decline in economic activity that spreads out over at least a few months.

According to Arthur Burns and Mitchell Wesley in their book Measuring Business Cycles (1946), "business cycle is the type of fluctuation that is found in the overall economic activity of nations and is expressed through business activity. The cycle consists of expansions that occur at about the same time in many economic activities, followed by similar general contractions and recessions, leading to the phase of the rise of the next economic cycle. This sequence of changes is repetitive, but not periodic. The duration of the economic cycle varies from more than one year up to ten or twelve years, and is not divided into smaller cycles with similar characteristics" (Burns & Wesley, 1946). The economic cycle consists of four phases, also known as stages or seasons, which are characterized by different patterns of economic growth and activity. These four phases are:

1. Expansion: This phase is marked by an increase in economic activity, rising employment levels, and growing consumer and business confidence. During an expansion, businesses are more likely to invest in new projects, and consumers are more willing to spend money. Economic growth is generally strong during this phase, and inflation may start to pick up.

2. Peak: The peak is the highest point of the economic cycle and marks the end of the expansion phase. During this phase, economic growth may start to slow down, and inflation may rise further. As the economy approaches full capacity, there may be shortages of labor and resources, which can lead to higher prices.

3. Contraction: Also known as the recession, this phase is marked by a decline in economic activity, falling employment levels, and decreasing consumer and business confidence. During a contraction, businesses are more likely to cut back on investment and hiring, and consumers are more likely to save money. Economic growth is negative during this phase, and inflation may start to fall.

4. Trough: The trough is the lowest point of the economic cycle and marks the end of the contraction phase. During this phase, economic growth may start to stabilize, and inflation may be low. As the economy starts to recover, businesses may begin to invest and hire again, and consumers may start to spend more.

These four phases of the economic cycle can last for varying amounts of time, and they can be influenced by a wide range of factors, including government policies, business cycles, and global economic conditions. Understanding the economic cycle and its different phases is important for investors, policymakers, and anyone interested in the overall health of the economy.

Some experts consider the Recovery phase as the fifth phase of the business cycle. During this phase, the economy, having already hit its lowest level, starts to show signs of recovery from the negative growth rate. As prices begin to fall, consumers tend to increase their consumption rate, leading to an increase in both demand and supply. Additionally, both individuals and organizations begin to regain their trust in making investments, while employment and production levels gradually start to rise.

Having examined the content of the economic cycles, we will now adduce the causes of an economic crisis through three different approaches. Three approaches have been identified to explain the causes of an economic crisis, namely those by Marx, Schumpeter, and the theory of "Social Structures of Accumulation" (Siddiqui, 2019).

According to Schumpeter's Long Waves theory (Schumpeter, 1939**),** a stagnant economy seeks to secure funds through the financial system, as it cannot raise them through the savings process. The flourishing period leads to an increase in demand, prices, and incomes, followed by a recession period once the process reaches its peak. In the Social Structures of Accumulation theory (Gordon, 1982) the relationship between employees and employers affects the production process, and an ineffective relationship can lead to a financial crisis. Gordon (1982) argues that labour relations play a significant role in the production process. The business cycle is divided into reproductive and non-productive cycles, and during recession periods, financially weak companies retreat, allowing stronger companies to claim a larger share of profits, which creates preconditions for wage reduction.

Marxist theory (Marx, 1867) holds that the capitalist society aims to increase profits by reducing production costs, which results in a reduction of wages. According to the Long Waves theory, capitalist economies experience cycles of growth and decline that last for several decades, driven by technological innovations and organizational structures (Kondratiev, 1926; Schumpeter, 1939). Due to increasing competition, the replacement of workers with technological equipment, and the liberalization of transnational employee movements, wages are pushed down, preventing the margin profit from decreasing for periods longer than 20-25 years.

In order to understand and explain the economic crises, other econimists developed different theoretical approaches. Their common orientation stemmed from the causes that may lead to economic fluctuation, concluding that the main causes consist of two factors. Those factors are endogenous or exogenous and may be characterized as “technical-economic” or “human-organizational-social” factors (Allen & Douglas, 2000). The exogenous factors mainly consist of wars, natural disasters, earthquakes, floods, fires, COVID-19, H1N1 virus, etc. (Allen & Douglas, 2000).

Reflecting on the external factors, Jevons suggested that high prices and crises in the wheat market occurred with the same frequency as solar spots, while

Schumpeter argued that innovations have a positive effect on the economy (Jevons, 1866; Schumpeter, 1939). Endogenous factors that can contribute to economic crises include excessive investments, decreasing purchasing power, fluctuating money supply, interest rate fluctuations, changes in productivity and labor supply, and falling margins (Allen & Douglas, 2000). On the other hand, the endogenous factors may include, among others, political and/or economic crises or even political instability in countries. Specifically, the excessive increase of investments during the rising phase, the decreasing purchasing power of the population in periods of economic recession, the fluctuation of money supply within the economy, the fluctuation of the interest rate, the productivity, the labor supply, the changes in the marginal return and the fall in the margin average profit (Allen & Douglas, 2000).

Asymmetric information can be a significant cause of financial crises. This refers to a situation where one party in a transaction has more and better information than the other party. In financial markets, borrowers often have more information than lenders about the risks and profitability of their projects. This can lead to lenders charging higher interest rates or excluding high-quality borrowers, as they lack the information necessary to assess the quality of the project. In some cases, lenders may choose to ration credit instead of raising interest rates to avoid adverse selection, leading to reduced access to credit for potential borrowers. Asymmetric information can also contribute to increased uncertainty, lower real estate market growth, bank panics, sudden market price reductions, and other factors that can lead to financial crises (Busuioc-Witowschi, 2010).

During an economic crisis, the negative effects can be manifested in unforeseen ways, creating an atmosphere of escalated intensity and high uncertainty. All sectors of society, including businesses, organizations, households, and governments, experience severe consequences. The impact of economic crises is primarily macroeconomic, affecting financial variables. However, economic crises are often associated with social and humanitarian crises, leading to losses in prosperity and pushing large sections of the population into poverty. The degree of damage caused by an economic crisis may vary depending on the time and place. According to the economists Marmot and Bell, the international trade, economic growth, and employment reflect the situation of the global economy. J

Joseph Stiglitz, another prominent macroeconomist, argued that the effects of the economic crisis differ not only between countries, where low and medium developing countries suffer more than developed countries, but also within countries, with manual workers and people with low education being affected more adversely than highly educated people in the middle and upper class (African Development Bank, 2019).

An economic crisis has multiple effects in every aspect of society such as economic, social, and psychological. At the social level inequalities are magnified and the feeling of uncertainty is born. High unemployment and unfair and unequal access

to the healthcare system and education represent another negative social consequence of the economic crisis. On a psychological level, more and more people suffer from mental disorders and anxiety due to the financial suffocation and uncertainty created by a financial crisis (Marmot & Bell, 2009). At the economic level, low liquidity levels are the effect of insufficient provision of any kind of loans, increase in interest rates, and the continuous reduction in revenues and investment activity. We observe loss and decline in income. Also, the inability to ensure sufficient funds for meeting financial needs results in increased debt and the economy is threatened with bankruptcy (Allen & Douglas, 2000).

Another pathogenesis of the economic crisis is the reduction of consumption due to low wages which leads to reduced production and finally affects negatively the national income. As a consequence, the trade balance exhibits reduction and the public debt is in an increase (Claessens & Kose, 2013). According to Cerra and Saxena (2008), financial crises tend to have permanent effects on output and the level of GDP. This means that financial crises can have long-lasting negative effects on the economy, including a decrease in output and GDP. Additionally, during an economic crisis, the government may increase taxes and bureaucracy to cope with the situation, which can lead to a rise in tax evasion by citizens. These factors can further exacerbate the impact of the crisis on the lives of citizens.

The Global Economic Crises

Even though financial crises exist throughout global history, each crisis has unique features, including its duration, intensity, causes, and impacts on the economy. The types of economic crises recorded in modern history include currency crises and financial crises, which are the most common types of crises experienced by the financial sector. Other crises include inflation crises, debt crises, oil shocks, and sovereign defaults (Reinhart & Rogoff, 2009; Cecchetti et al., 2009; Busuioc-Witowschi, 2010). Generally, an economy experiences periods of prosperity, stagnation, and crisis.

The conceptual framework of public debt refers to the situation in which a country enters due to the conclusion of bond loans and is unable to pay back. In this context, the debtor may be the state or public bodies and organizations subject to it in its control, such as utilities, and local government organizations. On the other hand, lenders can be foreign governments, international organizations such as the International Monetary Fund (IMF), the World Bank, etc., or individuals (banks, insurance funds, alternative investment agencies). A country can enter into a debt crisis when it cannot pay back its government debt which tends to grow and the tax revenues are insufficient, appearing to be less than its expenditures for a prolonged period.

Another kind of economic crisis is the **inflation crisis,** which refers to the constant percentage change in the general average level of prices of goods and services and factors of production of the economy over a given period (Statista, n.d.).

To determine this change in the price level, specific goods or services are selected while the products are weighted according to the impact they have on the average household budget. When it comes to the impact inflation has on the economy it can be supported that it plays a key factor in economic uncertainty and has multiple negative effects (Statista, n.d.).

In 1973, currency crises came to the fore and began to occupy economists' and politicians' attention after the suspension of the currencies pegging to the US dollar, as provided in the Bretton Woods agreement. The crises in Asia, Russia, Latin America, and Europe motivated many economists to focus their interest on the explanation and prevention of currency crises. The theoretical models of foreign exchange crisis that were developed are often categorized into first, second, and third generation (Howells, 2009). Currency crises can be defined as a sharp and large change in the real exchange rate of a currency which is mainly attributed to domestic economic policies and due to instability of international financial markets under the condition of a fixed exchange rate regime and a freely floating exchange rate regime (Howells, 2009).

Financial crises are a common phenomenon in global economic history, and they have a significant impact on the economy, society, and political landscape of affected countries. Financial crises can take different forms, and they are often categorized based on their underlying causes and manifestations. One way to categorize financial crises is to distinguish between banking crises and stock market crises. Banking crises are characterized by a sudden loss of confidence in the banking sector, leading to a run on banks and a liquidity shortage. On the other hand, stock market crises are characterized by a sudden and significant decline in the stock market prices, often triggered by a systemic shock or economic downturn.

The causes and dynamics of financial crises are complex and multifaceted, and they often involve a combination of endogenous and exogenous factors. Some of the most common factors that contribute to financial crises include overborrowing, excessive risk-taking, asset price bubbles, financial innovation, regulatory failures, political instability, and external shocks such as commodity price fluctuations or global economic downturns.

Empirical studies have shown that financial crises can have significant and long-lasting effects on the economy, including reduced GDP growth, increased unemployment, and increased public debt. According to Cerra and Saxena (2008), financial crises tend to have permanent effects on output and the level of GDP.

Business bankruptcies are a hallmark of crisis panics in the banks and the stock market and in general, the failure of the financial system of the country. Banking crises harm a country's real economy as they play an important role in its financial system. The creation of the stock market bubble is triggered by the credit union partnership, while the stock market bubble burst affects the banking sector and then the real economy (Bernanke, 1983). On the other hand, the stock market crisis is defined by

the dramatic fall in stock prices on a wide range of stock market securities for a certain period which leads to a new price level, that is much lower than the previous one (Kindleberger & Aliber, 2005).

The presence of stock market crises expands from within the country to the global level (Reinhart & Rogoff, 2009). The stock market crises are accompanied by the crash of the stock market bubbles. For example, the prices of assets, property, commodities, and bonds following the sharp rise in U.S. share prices during the second half of the 1990s, and their subsequent sharp falls in 2000 and 2001, continued their upward movements between 2002 and 2007 when the financial crisis occurred. Additionally, the chain of events may occur and vice versa, which means that the closure of a bank can cause the stock market to collapse (Reinhart & Rogoff, 2009). It is commonly argued that there is a close relationship between financial crises and the burst of the bubble in commodity prices. This is where a causal factor of an upcoming financial, banking, or stock market crisis can be found.

The Great Recession

The most impactful financial crisis occurred in 2007-2008 which played a crucial role in the formation of current economic conditions and still affects the economies at a worldwide level. The Great Recession, as it was named, was a sharp decline in economic activity while it was the largest economic downturn since the Great Depression. The globalized financial system is inextricably linked to markets, economies, and countries as they have developed relationships of dependence and interaction. Specifically, every imbalance the financial system experiences is transferred to the economy of each country, while at the same time, the financial crises of each country have a direct impact on the international financial system. Although the International Monetary Fund shares the view that we are experiencing the deepest post-war global crisis, other economists support that the Great Depression of 1929 and the financial crisis of 2007-2008 bear many similarities (Dupont & Passy, 2012). Both crises are global and are critical factors for the capitalist system as it has been shaped until today. There is a shared interest between analysts and economists which stems from the need to comprehend the causes, the depth, and which crisis was/is more impactful. On the other hand, others focus their interest on the analysis of the "lessons" we should have learned from the Great Depression to avoid and prevent future ones, or on a more realistic level cope with the present one (Lloyd, 2011). However, it is considered fundamental to put it in chronological order to provide a more complete view of the facts that led to shaping the current financial system.

In 1920, the U.S. market was experiencing a period of high levels of liquidity and prosperity. During the same period, new production methods and innovative products made their appearance (radio, cars, and electrical appliances), the fact that generated an equal need for banks to launch consumer loans and for consumers to demand consumer lending. The need for new product models, such as cars and radios

increased in the production sector to fulfill the demand and at the same time the need for more lending. In general, the economic situation before the crisis was at good levels, employment, production, and prices were rising. As a result, the existing prosperity led to the emergence of new investors in the stock market. Motivated by many factors such as their need for more consumer goods, greed, the bank provision of liquidity, and the general belief that there was a tendency to rise in stock prices, they borrowed to invest (Galbraith, 2000).

In 1926, the Dow Jones stock index was at 100 points. On September 3, 1929, the stock index reached its highest point, 381 points. However, in October 1929, the stock market bubble finally burst and investment collapsed. The real economy was not ready to handle and prevent the consequences of a stock market crisis. Investors could not afford to pay off their debts on time and businesses experienced great profit loss restricted elimination. The main features of the crisis became manifested immediately. Panic prevailed. Mass withdrawals and lack of liquidity for businesses led to bank collapse. As a consequence, reduction of production, losses, closure of companies, and increase in unemployment levels completed the scene of the general collapse of the economy which even the reaction of the central bank could not mitigate (Galbraith, 2000).

In 1970, the members of the Organization of Arab Petroleum Exporting Countries announced that they will not supply oil to the countries that supported Israel in its conflict with Syria and Egypt. This is when the first oil crisis makes its appearance leading the global financial systems of the most powerful countries to shake while insecurity and instability prevail. That fact in combination with the high degree of dependence of the industrialized countries on oil leads to inflationary increases in prices. A few years later, a second oil crisis affects the price stability as exports fall and prices soar.

In 1997, rapid growth accompanied by high investment activity constituted the driving force for the Asian economy. However, with the deficits observed in the Asian budget in combination with the inability to hold the exchange rate against the dollar, it is decided to suspend the operation of sixteen Thai financial companies. The inflow of foreign capital was immediate as foreign investors began to withdraw their capital. This has resulted in the devaluation of the currencies of Korea, Indonesia, Malaysia, Hong Kong, the Philippines, Singapore, and Taiwan, as well as significant losses in national financial markets and world trade.

Heading the financial crisis, which occurred in August 2007 and deteriorated rapidly during the fall of 2008, it seems that it first began as a financial crisis due to banking pathogenesis but it turned into a global economic crisis. According to Krugman (2008), the recent systemic crisis marked the deconstruction of the modern financial system, the impact of which had an immediate and great spread throughout the world affecting the global financial markets (Blankenburg & Palma, 2009). The

intensity of the crisis was such that every country experienced the consequences of the global crisis (Gamble, 2009).

The deregulation policy that was pursued for many years, the rapid increase in credit expansion, the complex financial products of companies, and the bank lending to unreliable borrowers led to a situation where banks could not properly assess and passed the risk to investors. At the same time, according to Wade (2008), the crisis gave rise to an unprecedented decrease in liquidity in the global financial markets and an increase in savings flows. In other words, the financial crisis in 2008 stemmed from banks' and financial intermediaries' liquidity and financing insufficiencies. The US attracted huge sums from the developing economies of Southeast Asia and China, which were used in the form of loans to finance consumption and housing credit. US banking institutions have resorted to subprime loan practices by granting mortgages to households without assessing their creditworthiness. The American central banks as well as immediate government intervention played a catalytic role in the early stages of the crisis. They were therefore forced to implement rescue plans and adopt important legislative initiatives to address the crisis by providing liquidity and lowering interest rates. The mass intervention concerned the occasional rescue of banking institutions. This means that they opted for a bailout of some banks while others were left to go bankrupt. In particular, while in March, US Federal Reserve (Fed) and J P Morgan Chase intervened to deter Bear Stearns from collapsing due to serious liquidity problems, they left Lehman Brothers with no rescue plan, especially because it was a high-risk financial institution. In the race of this financial race, Washington Mutual was left out and was placed in bankruptcy by the Federal Deposit Insurance Corporation (FDIC) because it faced a massive wave of bank withdrawals. In September 2008, investment bank Merrill Lynch ran a high risk to collapse but avoided bankruptcy thanks to the immediate response of the Bank of America by submitting a takeover bid.

Regarding the financial crisis in 2008, many economists attribute the outbreak of the financial crisis to multiple and at some point interdependent factors. In particular, the pre-existing pathogens of the financial sector, the global macroeconomic imbalances, the dangerous Bank portfolios, government deficits, excessive credit expansion, leverage, regulatory gaps, incomplete supervision, and the low-interest rates that were preserved for a very long time in the US contributed to this crisis (Blankenburg & Palma, 2009). Most of all, the prevailing perception about the causes that lead to new crises stem from the fact that economic operators do not learn from the past mistakes and repeat the same ones.

The first causal factor was the abolishment of the Glass-Steagall legislation and its replacement by the Gramm-Leach-Bliley Act, which marked the beginning of market liberalization and financialization, allowing financial institutions to expand their operations beyond those of conventional banking. The effects were severe since the financial markets' regulatory framework failed to protect investors. In response,

the national governments immediately proceeded to guarantee the deposits to avoid mass cash withdrawals from the banks and the nationalization of the banks, taking over their management and their losses. Despite the immediate response, Northern Rock was nationalized by the British government, Bear Stearns was sold to J.P. Morgan, Merrill Lynch, Fannie Mae, and Freddie Mac were acquired, Brandford and Bingley were nationalized by the British government, Fortis was partially nationalized, the US Federal Reserve and the European Central Bank cut key interest rates to historic lows to encourage entrepreneurship. However, the collapse and bankruptcy of the American Lehman Brothers in 2008 caused a liquidity crisis in the global banking system, freezing of money and capital markets, reduction of interbank markets, and insufficient financing of the economy. This fact indicates that financial institutions in possible failure have the potential to cause panic and threaten the stability of the entire global financial system which eventually occurred (Pagoulatos & Triantopoulos, 2009).

Furthermore, Taylor (2009) provided empirical evidence that "government actions and interventions caused, prolonged, and worsened the financial crisis. They caused it by deviating from historical precedents and principles for setting interest rates, which had worked well for 20 years. They prolonged it by misdiagnosing the problems in the bank credit markets and thereby responding inappropriately by focusing on liquidity rather than risk. They made it worse by providing support for certain financial institutions and their creditors but not others without a clear and understandable framework".

Securitization of innovative financial instruments and short-term mortgage lending (repo) made their appearance, a fact that played a key role in the building up of the upcoming crisis. In particular, a new mechanism was developed, and applied by banks which was the securitization of financial receivables (e.g. mortgages) into structured products. Banks stopped keeping these receivables in their assets and began to sell them as structured products in both domestic and international markets. In this way, the securitization of assets converted some previously non-negotiable assets (such as mortgages) into negotiable bonds. In other words, the financial institutions were able to create a composite product that stemmed from subdivided or combined loans to grant loans that were at the same time available to other institutions. The securitization of loans included the combination of different types of loans which were then restructured into complex investment instruments contained in a wider portfolio of "Asset-Backed Securities (ABS)" which were eventually converted into debt securities. In this way, banks, while selling their loans, were raising additional liquidity to provide new loans.

Allowing financial institutions to expand their operations beyond that of conventional banking, securitization changed the financing framework of financial institutions due to the transition from traditional lending (lending, holding loans) to the new way of financing (lending, restructuring, sale). The banks no longer took the

risk and thus an increased and uncontrolled liquidity was created, which increased the possibility of lending to non-creditworthy borrowers since they knew in advance that the loans would not remain on their balance sheet, while using the sale to produce new loans and therefore more profits. However, many of the investors did not know exactly what products they were buying and especially what risk they were taking. The calculation of risk was done by financial companies specialized in credit risk analysis, such as Moody's, Standard and Poors, and Fitch. Nevertheless, the control was incomplete as macroeconomic factors that would affect the real estate market were not assessed at the right time (Dullien et al., 2010).

In addition to the previous causal factor, the role of the credit rating agencies had a key role in the process of the financial crisis shaping (Lane, 2012). For a buyer to have access to "guarantee securities", he needs a kind of reliability, while another independent entity of the seller must ensure that these credit securities correspond to the good interest flows in the future. The most prominent rating agencies that were also mentioned previously are Moody's, Standard, and Poors, and Fitch. The main object of these agencies is to assess the risk of debts held by governments and companies. To make their decision, rating agencies supported 40% of their decision-making process to short-term and long-term factors. The short-term factors were constituted by the GDP per capita, the GDP growth rate, government deficit, and debt. On the other hand, the long-term factors that shaped their recommendations are the efficiency of the central government, external debt, foreign exchange reserves, and the history of bankruptcy. The remaining 60% of the factors that constitute their decision-making process remain unspecified since they can be attributed to psychosocial factors (Afonso, Gomes & Rother, 2011). Given that the factors that shape their decision stem from the agencies' best interest, discrimination and lack of transparency immediately turn the value of debt securities into junk (Lane, 2012). In addition, the lack of risk measurement instruments combined with the close interdependence of credit agencies with markets' movement made them unreliable with a reduced ability to predict accurately. Lastly, Moody's and Standard and Poors, together controlled 80% of the market and together with Fitch they reached 95%, hence the accusations of lack of competition and oligopolistic behavior prevailed.

Another important cause that contributed to the formation of the crisis is the movement of capital internationally. During the “bubble” period the U.S.A marked a negative sign in the current account balance (Karamitrou & Markou, 2014). The country began to exhibit deficits that could not cover its holdings and in order to cover these deficits began to receive capital inflows from abroad. At the same time and during the past 30 years, Asian countries such as China, exhibited high surpluses and had achieved tremendous economic growth through exports of industrial goods to the United States (Dullien et al., 2010). These exports led to huge surpluses in China's trade balance, which, however, did not supply domestic demand, but were placed in US bonds and other dollar-denominated securities, which kept the dollar relatively

high and US lending rates at relatively low levels. At the same wavelength, other oil-producing countries fluctuated due to their surpluses aided by high oil prices. In other words, foreign capital inflows by countries that accumulated surpluses in their Balance of Payment to the US had helped not only to stabilize the US dollar by investing their surplus funds in risk-free liquid government values but also to strengthen liquidity, restrict inflation and reduce lending rates which then reached 1%. But reality was different. The more dollars of surplus countries were devalued, which enabled them to participate in the globalized market, the more the bubble in the United States expanded.

Another factor that played a key role was the uncertainty that prevailed after the 9/11 attack in New York which caused instability and fear in the financial markets. To prevent a possible collapse of the domestic and consequently global economy, the US implemented interest rate cuts and a general easing of fiscal and monetary policy, which encouraged borrowing (Dullien et al., 2010). All these measures were implemented aiming at boosting the economy. For the following years, there was a period of historically low-interest rates resulting in a continuous increase in house prices. At the same time, low-interest rates have led savers to switch to more profitable, high-risk investments. Subprime lending was granted to low-income clients with reduced chances of repaying the loan while they were characterized as insolvent borrowers. When interest rates began to rise and house prices fell, many borrowers were unable to meet their loan repayment requirements. The subprime loans crisis extended to bonds, collateralized debt obligations, and insurance and reinsurance companies, eventually creating financial suffocation (Claessens & Kose, 2013). By 2005, more than 22% of the US was given to high-risk borrowers, while this percentage in 2007 rose to 26%, the high levels in which interest rates fluctuated were speculative tools. In 2008, nearly nine million American homeowners were found to owe more than the total value of their property (Afonso, Gomes & Rother, 2011). An increasing number of homeowners have been unable to repay their loans, while the value of home loans has declined (Obstfeld & Rogoff, 2009). As a result, in 2007, the economic crisis turned into a global crisis.

High leverage was proved as an important factor that contributed to the crisis. The term leverage refers to the phenomenon in which the lending of a financial institution is greater than its assets, while at the same time exhibiting little equity. High leverage and even short-term borrowing have been the cause of the rapid spread of the crisis from the purchase of subprime loans to the markets of many other assets. In addition to households, many traditional or investment banks also had high leverage. The sudden fall in assets affected directly the capital markets which began to record losses. This had a consequence for the financial institutions to reduce or even deny short-term financing to the investment banks, the fact that led the latter to sell their assets, restrict the provision of new lending, and sell their assets such as shares and bonds (Matsas, 2012). In addition, the refusal to borrow transferred the crisis to

the real economy. About $ 1.7 trillion is the cumulative losses, which have been accepted by financial institutions in their balance sheets, although they are to some extent offset by corresponding capital increases. In June 2008, impairments reached $ 698.2 billion. In June 2009, they more than doubled to $ 1,662.7 billion and in mid-December 2009 were at $ 1,703.4 billion. In June 2008, the gap between impairments and new capital inflows was $ 314.6 billion.

According to Kindleberger and Aliber (2005), the failure of products to sell is the main sign of the upcoming crisis which results in a continuous decline in profits. Insufficient liquidity generates the need for business and consumer loan demand, urging banks to impose high-interest rates and implement stricter criteria, which subsequently leads to low investment activity and restriction of consumer credit. In general, an economic crisis affects a country's economic activity to a great extent while continuous reduction of GDP level and the reduction of revenues and investments may lead to a lack of liquidity. As a result, the state is threatened with the inability to secure the economic resources to meet the fact of the financial needs that may lead to debt increase or even bankruptcy (Allen & Douglas, 2000).

Concluding, from 2002 through 2007, the highest global economic growth of the financial sector was noticed. However, that prosperity was only a bubble that would end up in the biggest economic crisis of all times, the effects of which are not and will not be clear until this crisis comes to an end but are considered more severe than those of the Great Depression of 1929 (Dupont & Passy, 2012).

Conclusion

Concluding, this paper provided an overview of the conceptual framework of economic crises using the economic cycle, and identified causal factors such as restrained funds and the relationship between employees and employers, as well as endogenous and exogenous factors and information asymmetry. Economic crises have widespread effects on all sectors and can lead to macroeconomic and banking system imbalances, as well as social and psychological instability. The financial crisis of 2008, which began with the bursting of the housing bubble in the US, was the most impactful crisis due to unprecedentedly low global interest rates, loose monetary policy, global imbalances, microeconomic distortions, and misstatement of risk and loss regulation. The collapse of Lehman Brothers in September 2008 marked the depth of the financial crisis. For the purpose of giving the reader a more comprehensive understanding of the philosophical underpinnings of the economic crisis, a bibliographic survey of the field was offered. Particular attention was placed on the nature of the economic crisis, the causes and potential impacts of the economic crisis, as well as the various economic crisis types that preceded the devastating financial crisis of 2008. Finally, an effort was made to investigate the start and major incidents that caused it to start and expand throughout the entire planet.

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