The Financial Crisis of 2008: Who’s to Blame?

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Many individual Americans adversely affected by the downturn in the economy beginning in 2008 wanted to know then, and they want to know now, the cause or causes of this crisis, especially since it has been frequently compared to the Great Depression of the 1930’s, the bellwether of financial crises. Surely such a global financial event must have identifiable causes—causes as big and as obvious as the lost retirement funds and savings, the high unemployment figures, and the anemic economic growth that have resulted from the 2008 crash. What federal government deficit and debt, what Wall Street firms’ fiascos, what International Monetary Fund madness, what World Bank blunders are most to blame?

Most financial experts don’t provide us with any real help in finding an answer, whether there is a single cause or multiple causes. In fact, according to Weisberg (2010), “Historians are still debating what caused the Great Depression, so it’s not likely this argument will be settled any time soon” (p. 19). So, while Americans search unsuccessfully for the villain or villains in this tragedy, the real culprit remains at large, hiding under their very noses. The steep downturn in the economy in 2008, and the sluggish recovery since then, can be blamed mostly on the individual American who was financially unprepared to lose a job, who lived beyond his or her means, and who panicked well after the real crisis was over.

How many economic downturns in American history do financial experts need in order to prepare themselves and the average American for the next dip in the cycle? The financial rollercoaster ride in America has been a long one, from various banking and monetary value panics throughout the 19th century and early 20th century, through the Great Depression of the 1930’s, to the inflation, deflation, stagflation, boom-and-bust hills and valleys of the last 50 years, culminating, so far, in the recession of 2008 and its lingering aftermath. Unfortunately, a
sort of collective and self-imposed amnesia often settles over the American populace. They see only the blue skies of prosperity when there is good financial weather; they forget that the weather changes, and dark clouds—sometimes hurricanes or tornados—will inevitably appear.

The causes for these financial peaks and valleys are as varied as the number of experts one questions. The list of prime suspects includes greedy Wall Street corporations/manipulators and their equally greedy and willing clients. According to an April 13, 2011, United States Senate Subcommittee Report entitled *Wall Street and The Financial Crisis: Anatomy of a Financial Collapse* (2011), “[H]igh risk lending by U.S. financial institutions; regulatory failures; inflated credit ratings; and high risk, poor quality financial products designed and sold by some investment banks, contributed to the financial crisis” of 2008 (p. 639). The members of this subcommittee conclude, and rightly so, that the finger of blame for the financial crisis cannot be pointed at one cause but at many causes. What is also clear from this conclusion is that many different people and institutions cooperated in actions that led to the crisis. Such a willingness to cooperate often muddies the search for a primary cause since blame is shared, and perhaps therefore lessened in degree for any one participant, due to the number of the participants involved.

Also often targeted for blame have been irresponsible government spending programs and equally culpable elected officials presiding over the ever-increasing deficits from year to year and the accumulated debt of over 14 trillion dollars in 2011. Interestingly, Gelina (2010) notes that the financial crisis that hit Americans in the fall of 2008 did not even have to happen. She characterizes the crisis not so much a “failure of markets” but “a failure by government to understand its proper role in markets” (p. 22). The author contends that for more than half a century prior to our current economic crisis, there existed “a sensible system of rules and
boundaries” that the government ignored during this crisis (p. 22). Ironically, it was the U.S. government itself during the Great Depression that had imposed certain regulations on the banking industry (the Federal Deposit Insurance Corporation in 1933) and on Wall Street (the Securities and Exchange Act in 1934), respectively, “to allow bad banks to fail in an orderly fashion without imperiling the rest of the economy” (p. 23) and to “require companies that wished to raise money by selling stocks or bonds to the public to explain—soberly, clearly, and regularly—the financial, business, and economic risks that the companies and their investors faced” (p. 25). Gelina explains that during the 1980s, intricately connected global financial companies could no longer be restrained by such government regulations. Government officials were too slow to recognize the significance of this financial evolution, especially since these companies lobbied Congress and made contributions to the campaigns of many of its members. Before long, she explains, “[t]he financial industry... [was] buoyed by an implicit government subsidy,” and, as a result, politicians could no longer effectively enforce the regulations their counterparts of the Great Depression had put in place (pp. 25-26).

Additionally, some have cited as causes for our current financial mess the fast-and-loose banking practices—ostensibly the attempts by compassionate bankers to empower more and more Americans to share in the American dreams of housing and transportation. Weisberg (2010) believes that we have an important lesson to learn about “our financial markets [which] need stronger regulatory supervision to prevent bad bets by big firms from going viral” to prevent the crisis from happening again (p. 19). Weisberg further notes that “[t]he only near-consensus” about the cause of the 2008 financial meltdown is that “the housing bubble burst [in 2007], leading to a high rate of defaults on subprime mortgages” (p. 19). A domino effect ensued, he says, which “doomed Bear Stearns in March 2008 and then led to a banking crisis that
fall” (p. 19) What happened next? The author contends, “A global recession became inevitable once the government decided not to rescue Lehman Brothers” (p. 19). The fall of Lehman Brothers marked the largest bankruptcy in American history. The stocks on Wall Street reacted to this failure by falling the way they did after the terrorist attacks of September 11, 2001. The panic was a reaction to the fact that an investment bank as large as Lehman Brothers affects many individuals and other financial firms, globally, that relied on Lehman Brothers to further support their borrowing. When an investment bank as large as that falls, so do many of the smaller firms—and people—that relied on it. Further complicating the fall of Lehman Brothers was that it had enormous debt associated with subprime lending in the mortgage industry. The owners of those mortgages—both individuals and banks—lost this investment bank’s primary lending support.

To a great extent, many of these causes are in fact responsible for the systemic spending illnesses suffered by our leaders in government and finance. The complicity of high finance and big government is succinctly summarized by Boone and Johnson, who note:

There were many factors that led us to the financial crisis of 2008—dangerous derivatives, irresponsible ratings agencies, negligent regulators—but one was more important than the rest. We now know it as the “too big to fail” problem. What brought the economy to the edge of disaster wasn’t only that financial institutions had made rash bets on lousy investments, but that those institutions were so massive that when their bets went bad, they threatened to take the rest of the economy down with them. That’s why Washington was forced to come to the rescue with hundreds of billions of dollars in bailouts for the likes of AIG and Citigroup, and why, when Washington turned to the task
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of making our financial system safer, President Obama vowed, “Never again will the American taxpayers be held hostage by a bank that is too big to fail.” (p. 20)

The knowledge and power of these men and women in government and finance are often corrupting influences, leading them to see only the small picture, the short term, enriching themselves and their friends at the expense—literally and figuratively—of great masses of individual workers in America whose ignorance, gullibility, and daily toil prevent them from seeing themselves as anything but victims of large, unmanageable forces in their lives. Their votes and investments always seem to allude the prosperity—even the financial stability—they seek.

How reassuring to Americans then, are the conclusion made by men and women in government about the causes and effects of the financial downturn of 2008? Senators conclude in Wall Street and The Financial Crisis: Anatomy of a Financial Collapse (2011) that “[t]o prevent investment bank abuses and protect the U.S. financial system from future financial crises,” several things must happen, including “Review Structured Finance Transactions” by “[f]ederal regulators…to identify any violations of law and to examine ways to strengthen existing regulatory prohibitions against abusive practices involving structured finance products” (p. 639). Other recommendations include “a meaningful ban on proprietary trading” to better “serve clients” and to “reduce risk” (p. 639). Finally, “Conflict of Interest Prohibitions” as well as a study of “Bank Use of Structured Finance,” says the committee, will increase the oversight of federal regulators in “the role of federally insured banks in designing, marketing, and investing in structured finance products with risks that cannot be reliably measured” (639). But shouldn’t Americans be wary of the help of a federal government whose regulatory role in the financial markets has been increasing for decades but which can’t prevent the kind of pain and hardship
left in the wake of the 2008 recession? Perhaps, instead, Americans should look to themselves for the causes—and the preventions—of such crises.

Admittedly, financial experts have been telling Americans for years to have a six-to-eight months reserve of disposable cash on hand so that if a job is lost unexpectedly, an individual financial crisis won’t ensue. Instead, many Americans live paycheck to paycheck. So, when an economic downturn occurs—large or small—as part of a regular business cycle, Americans who are out of work have to find a job immediately, and they are often unable to do so. Whatever small savings they have are rapidly depleted, and then they begin to borrow on credit cards simply to pay for groceries and housing. Their inability to pay for these items—because of lack of cash reserves while they look for another job—has a cascading effect on the economy since they don’t buy the amount of groceries or housing or consumer items that they did before, and they sometimes lose their homes. So, what could have been an easily weathered downturn, large or small, in the economy becomes much worse because of the unprepared worker/consumer.

The financially unprepared American is also most likely a consumer who has taken some of the money he or she should have saved for a rainy day and instead leveraged it to buy the house, car, clothes, jewelry, or vacation that he or she really can’t afford. Credit cards and home mortgages are often abused to borrow cash for items desired but not needed. When the normal financial downturn occurs for these Americans, the cascading effect occurs again because the unneeded items, in one form or another, must be returned, if possible, or sold for well-below their market value. The sellers who are stuck with the returned products now have a glut of products to sell and often find it hard in an economic downturn to attract customers, even when they offer “deals” to break even. So, these merchants—and their employees—suffer because of the overspending of the individual Americans.
Finally, the financially unprepared, overspending American who manages to survive the economic downturn and find another job is once burned and twice shy: even when economic indicators suggest that a recovery is underway, this American is hesitant to get back into the financial game. Instead of spending money even in a reasonable way, he or she becomes a hoarder of cash that sits in the bank or mattress “just to be safe.” Glick and Lansing (2011) explain,

During the boom years of the mid-2000s, the combination of declining saving rates and rapidly rising household debt allowed consumer spending to grow much faster than disposable income, providing a significant boost to the economy. Recently however, the rebound in the saving rate has coincided with a reduction in household debt—a deleveraging—that has acted as a drag on consumer spending and the economy (p. 1).

This lack of enthusiasm to spend—also known as low consumer confidence in the economy—can prolong an otherwise short downturn, turning it instead into a longer downturn, or double-dip downturn, because of the lack of faith in the economy and in fellow Americans all along the buying-selling chain.

Many would argue that holding cautious American consumers responsible for a prolonged economic downturn is not fair. Why should these consumers be quick to return to confident buying of the past when they were probably imprudently spending back then too, even if it did help to fuel a growing economy? Slow and steady growth in the economy, after all, while less exhilarating, provides the kind of stability that most economists say we should try to create. Nevertheless, the too cautious consumer shows a fundamental lack of faith in the economy, however he or she justifies this caution, and such caution can delay the return to a more robust economy.
Can Americans who formerly didn’t save, who overspent, and who then panic change their ways? Can they imagine and then take even greater control of their financial destinies? Some experts say yes. For example, Glick and Lansing (2011) explain that “[f]ollowing a 20-year decline, the U.S. personal saving rate bottomed out at around 1% in the third quarter of 2005. Since then, the rate has been trending upward, reaching around 6% in the third quarter of 2010” (p. 1). Perhaps Americans will continue to follow these better financial practices. And there is additional reason to hope. For example, according to Palmer (2009), “Americans have put themselves on a budget” (p. 57). This author notes that instead of spending money frivolously on food, drink, and vacations, Americans are saving that money. Palmer explains that personal savings rates are reaching levels not seen in a decade, and that credit card debt is falling. A majority of Americans, this author says, are spending less money this year than they did the year before. Palmer asks hopefully, “Will that moderation continue as the economy strengthens?” The author answers tentatively that “[i]nterviews with economists, consumer experts, and consumers themselves suggest that for at least a significant number of people, recession-inspired behavior is here to stay” (p. 58). A Senior Economic Analyst for Business News Network agrees, noting that “from a peak of 130 percent in 2007, the household debt-to-income-ratio in the U.S. fell to 116 percent last year” (Nazareth, 2011). That’s good news, the author says, because this reduction of debt load by American consumer could not only sustain an economic recovery but help make the next dip in the economy less devastating.

The irony of these events is that Americans fear economic downturns, believing that such events are completely out of their control when, in fact, as these three causes show, their actions to a great degree can prevent or lessen the effect of natural downturns due to supply and demand fluctuations (downturns we can’t control). The Stoic virtue of being courageous concerning
things we can’t control (since we can do nothing about them) and being cautious concerning
things we can control (since our actions are important and define who we are) is often perverted
by the financially unprepared, overspending, panicky American consumer. Why? Because
sometimes Wall Street greed, subprime mortgage debacles, giant Ponzi schemes (for example,
Bernie Madoff and company), and massive government spending are, to a great extent, out of the
individual American’s hands; however, he or she could courageously face such events by
managing money wisely, by living within one’s means, and by not panicking when financial
times get tough.


