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Lessons from the great recession: need for a new paradigm?

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Abstract

The ongoing sovereign debt crisis in Europe and U.S. is challenging the conventional wisdom and is creating fears of a double dip recession in 2012. Massive levels of debt and consumption beyond means and speedy financial innovation with lax regulation has put major economies in a deep hole. Monetary policy with ease in rates had been ineffective to say the least in generating new jobs in last few years when interest rates were kept at near zero level since 2008 in U.S. Fiscal stimulus again targeted the undisciplined financial sector which did not use the stimulus for extending credit to the private sector as much as was required. With business cycle fluctuations, mounting consumer and fiscal debt is unsustainable and one lesson of the crisis is that business cycles are for real and here to stay. The securitization of consumer debt magnified the losses and created negative unjust effects on savers and taxpayers which had nothing to do with the mess in the first place. In this backdrop, a new paradigm is needed which put the focus back on productive enterprise, brings recovery with job creation, limit speculative financial institutions and instruments and improve corporate governance by influencing the incentives more deeply.

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