Macroeconomic Policy Context of Similarities and Differences of the Great Depression and the Current Global Economic Crisis

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Abstract

The objective of the article is to identify similarities and differences between the Great Depression and global financial and economic crises in period 2007 – 2010. The analysis examines a hypothesis that the main causes of financial and economic crises include unbalanced developments of the macroeconomic sphere as well as existing weaknesses of banking systems, which often do not evolve in line with the development of economy fundamentals. The article is going to inspect three areas: (i) What economic policies and trends were registered in the pre-crisis period in order to identify the main causes of economic fluctuations; (ii) How economic policies responded to the course of the financial and economic crisis; (iii) What was the effect of financial crisis on the real economy development. The main task for after-crisis periods is to improve stabilization of macroeconomic policy, bank risk management system and also system for monitoring and analyzing the business cycle.

Keywords: *financial crises, economic crises, business cycle, credit cycle, gross domestic product, macroeconomic imbalance, unemployment, monetary policy, national debt, demand shock, supply shock, interest rate, financial stability, asset prices*

JEL Classification: O11, O16, O23

Introduction

Historical experience shows that the most common causes of a decline in economic activity were financial crises and price shocks in global commodity markets. Due to a higher frequency of both these causes of economic recession,

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we nowadays have a certain level of knowledge of how the initial impulse to the economic recession started, how the monetary authorities responded and how long or deep the recession was. Price shocks in commodity markets appeared in every decade after 1970, being most significant in the 70s and in 2008. Among their causes was a disharmony between supply and demand in global markets. However, the impacts on inflation and performance of the economy differed according to the strength and length of a price shock and responses of economic policy were not unambiguous.

There were important financial crises mostly in the 90s, but they were limited to certain countries or regions only, e.g. in Finland, Japan, Mexico, Russia, Southeast Asia, the Czech Republic, Brazil, Argentina (Dalsgard and Elmeskov, 2002). The combination of both fixed exchange rate and high interest rates representing a significant incentive for the inflow of foreign capital were among the major causes of financial crisis in this period. The exorbitant liquidity of banks led to less cautious credit granting and thus to the increase in unpaid debts. Thus an extraordinarily high number of credits were a major cause of these financial crises.

The objective of this article is to deepen the knowledge of causes, the course, and impacts of the global financial and economic crisis. The analysis focuses particularly on identification of the role played by economic policy, credit cycle and macroeconomic imbalances during the crisis. The main goal of the investigation is an assessment of several groups of interactions: (i) which major trends in the development of the economy and economic policy were noticed in the pre-crisis period and which of them contributed to the emergence of the economic crisis; (ii) how economic policies responded to the increase in the recession forces during the financial and economic crisis; (iii) what impacts on the development of real economy the financial crisis had; (iv) what similarities and differences between the Great Depression and the current financial and economic crisis can be identified; (v) what should become subject to corrections in economic policy in the after-crisis period.

1. Methodological Backgrounds

The approach to the analysis of crisis situations in the economy is based on the conceptual boundaries of financial and economic crises. According to the definitions (IMF, 1998) a financial crisis is understood as follows: ”systemic financial crises are potentially serious disruptions of financial markets which together with worsening of the market ability to function efficiently may have strong unfavourable impacts on the actual economy.” There is also another definition

available, which explains a financial crisis as instability of financial markets showing significant problems in non-liquidity and insolvency of market players.

Financial crises can be classified as currency crises, banking crises and debt crises, which may occur in various combinations. Currency crisis (Krugman, 2000) is usually understood as a shift of assets from one country, where the performance of the economy and financial stability is threatened to assets in foreign currencies which results in major devaluation of the currency concerned. A banking crisis, as defined by the IMF, is a real or potential run on banks caused by public concerns about the ability of banks to pay their liabilities. A standard sign of such banking crisis is either an outflow of deposits and subsequent postponement of debt repayments or a threat of such postponement does not appear thanks to powerful state intervention. A debt crisis means a disability of a country to pay foreign or governmental debts. A standard definition of an economic crisis is a deeper and longer decline in the performance of an economy measured by GDP.

The main objective of the presented analysis is a relation between the rise in the performance of the economy, economic policy, credit cycle and macroeconomic balance. These relations are derived from the logic of a relation chain of capital flow in the global economy and form a basis for a methodological approach to monitoring and analyzing financial and economic crisis.

The basic idea of the analysis is the fact that the existence of bigger imbalances or irregularities in long-run trends on the supply and demand side of the economy has pro-cyclical consequences for economic growth. This concept was used to assess relations between economic policy and economic growth. Creation of conditions enabling a relatively consistent development of four main macroeconomic goals i.e. in the field of economic growth, inflation, external economic relationships and employment belongs to the basis of a stabilization policy. This means to avoid development of some macroeconomic goals at the expense of other targets which would become a narrow point or a barrier to sustainable economic development in the intermediate or long term. If monetary and fiscal policies are set expansively, its effect is predominantly pro-cyclical.

The analysis of a global financial and economic crisis focuses on such components of economic development which are connected with the course of a business cycle both in its upward and downward phases. Sets of three indicators are used in the analysis. These are indicators of economic performance, macroeconomic balance, both inner and external balance, and indicators of financial vulnerability. Applying them, one assumes that the bigger the problems are registered in macroeconomic unbalance and financial vulnerability, the bigger the slump in the growth of economic performance may be.

2. Pre-crisis Situation in the 1920s

Having recovered from the consequences of the World War I, the economic development in the 20s of the last century was characterized by a long lasting dynamic economic growth. In 1920 – 1929 the real GNP grew by an average year-to-year pace of 4.2%. Favourable conditions both on the supply and on the demand side of economy belonged to the supporting factors. It was mostly the development of new industries that contributed to the growth in economic performance. In 1921 – 1928 the industrial production in the USA grew by 4% a year, in 1928 – 1929 even by 15%. Epoch-making inventions such as washing machines, refrigerators, vacuum cleaners, irons, radios, air-conditioning, cars, etc. played a key role. It was also a low rate of inflation thanks to which the position of durable goods in the structure of consumption was significantly strengthened. Among other features of macroeconomic development was also the fact that the USA strengthened their position of a leading global exporter particularly when they took over the first position in the export of final goods of manufacturing industry. The USA also maintained the position of a major global investor and creditor.

Significant surpluses were created in American balance of foreign trade in goods. This was supported not only by competitiveness of the economy which was not weakened by the war, but also by customs protection of American market with industrial goods introduced in the beginning of the 1920s as a response to the emergence of after-war recession.

Fiscal policy was set to generate a slight surplus in budget receipts over expenses. This was achieved with the help of a threefold tax reduction focused particularly on reduction in income-tax progression of physical entities and growth in tax revenues of the booming economy. Pursuing budget balance thus did not get the economy into debt.

During the 1920s the capital market started to play a more and more important role in the American economy. While in 1921 there were about 40 investment companies operating in the capital market, in 1927 their number exceeded 300. Not only professionals and big investors, but also broader public were interested in investments in the securities market. Rapid growth in the securities market was encouraged by offering credits, where it was enough to pay 25% of the price and the rest could be borrowed, while newly bought securities used to be pawned as a guarantee for new purchases. It took Dow Jones securities index almost 22 years (1906 – 1927) to climb from 100 to 200 points. However, it added another 100 points in only one year and in 1929 it was heading further up. In the last quarter of the 1920s it started to be obvious, that there was a speculative bubble not corresponding with the fundamentals of the economy.

By the end of the decade incentives for further investments started to decline, since the increased capacities of companies started to be excessive. Domestic investment and consumer demand started to lag behind the supply, stocks started to accumulate and in 1929 they reached three times the level of the preceding year.

Thus exorbitance of industrial and construction capacities and saturation of consumer demand belonged to the aggregate characteristics of a starting mechanism of recession forces. Big dimension of risky credits of many American commercial banks belonged to supportive forces. From macroeconomic policies it was a non-adequate interest policy that contributed to launch the crisis (Bernanke, 1995; Friedman and Schwartz, 1963). Such an interest policy switched between below-average interest rates, which supported the economic growth and immoderately high rates around 6%, which violated the financial stability and excessively slowed down the growth in the performance of the economy. Application of currency policy with the help of the gold standard, which obstructed a bigger elasticity in adjustments of the currency to changed economic conditions, had a similar influence (Eichengreen, 1992).

3. Pre-crisis Situation in 2000 – 2007

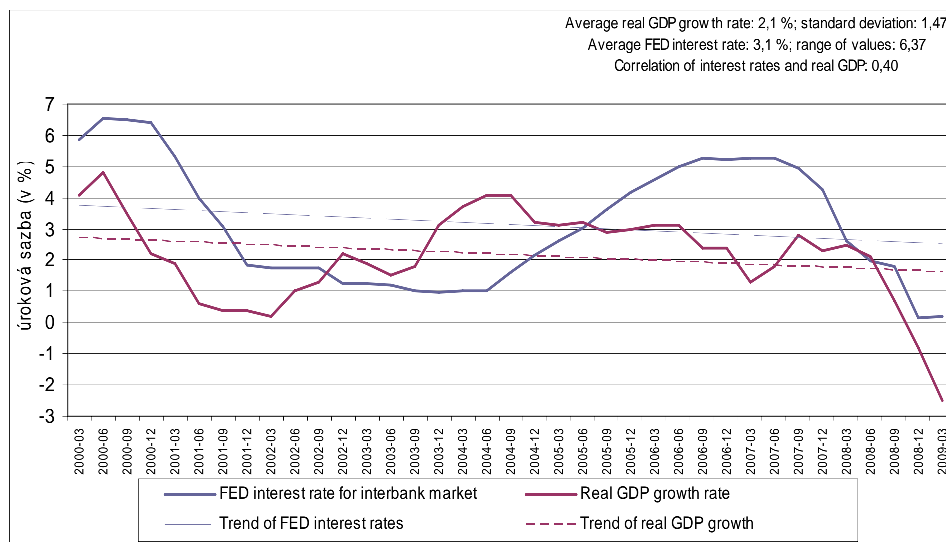
The development of American economy with its leading position in global economy played the most significant role in the pre-crisis period. The economic growth in the questioned period was characterised mainly by fluctuations in the achieved performance and a slower average pace of growth compared to the previous decade. Growth stability was disrupted by a higher number of external shocks. Among them were rising imports of cheap goods from Asian economies, geopolitical conflicts, strengthening terrorism, oil shocks, frauds in accounting and bankruptcies of airlines companies.

An average pace of year-to-year growth in GDP in the USA was 2.3% in 2000 – 2007, which was by 0.6 percentage point higher than in the Euro-zone. The macroeconomic development of American economy was influenced predominantly by expansionary monetary and fiscal policy supporting domestic both consumer and investment demand. Among the supportive monetary conditions one can mention is mainly the policy of low interest rates used in 2002 – 2004 (Figure 1). This should have deterred the recession, which threatened after the terrorist attacks on the USA in 2001. However, in its consequences this interest policy generated two negative effects. First it started a credit cycle and imbalance in the housing market and at the same time deposits of foreign investors started to be transferred into territories with a higher interest rate. A subsequent negative impact of this credit expansion was the extremely high number of credits

offered by banks. A mortgage share on indebtedness reached 71% of the GDP in 2005, while in Great Britain and the Netherlands it was even higher and it started to be close to 100% of the GDP (Corden, 2009).

Figure 1

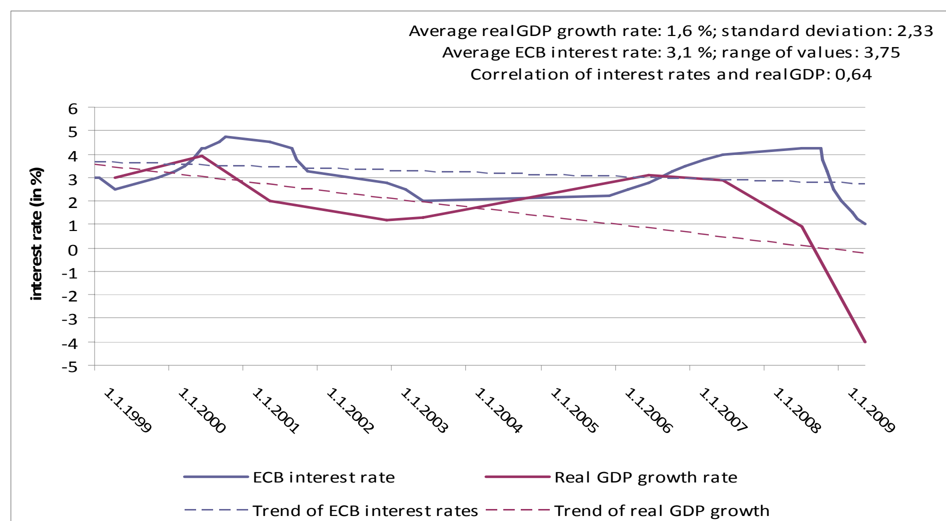
GDP and Interest Rate in the USA



Source: FED (2009); own calculations.

Figure 2

GDP and Interest Rate in Euro Area



Source: ECB (2009); Eurostat, Statistics (2009); own calculations.

A slower pace of GDP growth in the EU was influenced by substantial strengthening of Euro against American dollar, which damped down export and production performance of European economies. A 2.3 percentage point growth in interest rates in 2005 – 2008 also played an important role together with shifts in investment activities from advanced economies into less developed ones, where the yield from the capital was much higher thanks to a low wage level (Figure 2).

3.1. Increase in Macroeconomic Imbalance

One of the characteristic features of the development of economy in the USA in 2000 – 2007 was the rise of external and internal imbalance accompanied by the emergence of a price bubble in the housing market. External imbalance grew in the long run from the beginning of the 1990s. After 2003 the deficit of the current account of the balance of payments started to oscillate above the value of 5% of the GDP (Table 1). Foreign investors consider this value an indicator signalling problems with sustainability of funding economic growth in an ensuing period. This was also one of the reasons of the outflow of foreign capital from the USA, which negatively influenced weakening of American currency.

T a b l e 1

External Balance (Current Account Balances as a Percentage of GDP)

	2001	2002	2003	2004	2005	2006	2007	2008
USA	–3.8	–4.4	–4.8	–5.3	–5.9	–6.0	–5.3	–4.9
Euro area	0.1	0.6	0.5	1.2	0.5	0.4	0.3	–0.4

Source: OECD Economic Outlook (2009).

After generating surpluses in the mid-1990s the budget of public finance also started to have a deficit character. Admittedly, budget receipts were stable, however, expenses started to grow due to war and terrorist events. A substantial speeding up of the growth in the total debt including both private and public sector belongs to the most important features of the development of American economy. In 2008 the total sum of debt reached USD 57 billion, which was a record sum and at the same time also the highest rate of indebtedness in the history. It represents USD 186,717 per head, which is USD 32,104 more than in the previous year. At the same time the total debt increased by 3 billion and it grew three times faster than the GDP. The growth in the performance of the economy is thus more and more dependent on the growth in the indebtedness. Since 1990 the debt has risen by 79% (USD 45 billion), which means that the primary driving force of the growth was getting into debt instead of productive activity.

Empirical data shows that the rate of debt was 499% of the national income in 2008 and from a long-run view it tends to increase. In 2007 there were a USD 6.28 of the debt per unit of output (1 dollar GNI) and the efficiency of an increment of a debt unit showed a negative value. Share of foreign investments on the growth of GNI has been increasing steadily, in 2008 foreign sources participated in debt funding with USD 13.6 billion, which is almost one fourth of the total debt (Hodges, 2009). China and Saudi Arabia play the most important role. Thus the USA has been gradually losing control over the development of their economy.

Profit structure of American economy changed significantly. Growth in the indebtedness of the country brought high profits for companies in financial sector. While in 1980 the share of bank profit was 18% of all profits in the economy, then in 2005 it was already 38% of the total value of profits in the entrepreneurial sector (Foster and Magdoff, 2009). This sharp increase in profits in banking edged out yields of industry from front positions and financial sector thus became the most flourishing industry of the national economy. Returns on banks´ own capital (ROE) were high and fluctuated in double digit numbers.

Europe experienced a more favourable development in macroeconomic unbalance. It concerned mostly external balance, since the current account deficit of the balance of payments in advanced European economies did not reach critical values except for several countries in transition. A higher number of advanced countries achieved surplus balance. Examples were Austria, Denmark, Finland, Germany, the Netherlands, Belgium, Sweden, Luxembourg, Norway and Switzerland. This gives evidence about very good results of these countries not only in the foreign trade in goods and services, but also in the transfer of yields from direct foreign investments.

However, Europe as well as the USA had to face budget imbalance. Most countries showed deficits of public budgets, which did not coincide with a growth phase of a business cycle. This lapse led to the increase in indebtedness of the government, which future generations will have to pay back. Nevertheless, total average sum of public deficits in Euro zone was still substantially lower than the deficit of American economy. Denmark, Sweden, Finland, Norway, Luxembourg and Switzerland belonged to a smaller group of countries with budget surplus and thus with the ability to create reserves for crisis years. The following review of budget balances shows that in the USA and most European countries economic growth was reached with the help of the growth in indebtedness. The main cause for this situation was expansionary fiscal policy responding first of all to the need to incur growing expanses of pension and health care systems connected with aging of population.

Table 2

General Government Financial Balances (Surplus or Deficit as Percentage of Nominal GDP)

	2001	2002	2003	2004	2005	2006	2007	2008
USA	–0.4	–3.8	–4.8	–4.4	–3.3	–2.2	–2.9	–5.5
Euro area	–1.8	–2.6	–3.1	–3.0	–2.5	–1.3	–0.6	–1.4

Source: OECD (2009).

A certain shift towards balanced trends won its importance in the development in the labour market, where in the given period employment grew and unemployment declined which was true to a larger extent about the USA but about European countries as well. This was caused not only by economic growth but also by the growth in part-time jobs, shortening of working hours or requalification processes, which in their consequences diminished the gap between supply and demand in the labour market.

Up to 2007 there was a favourable trend in the development of consumer prices, where low and stable inflation was registered for most of the period monitored. This situation gave evidence about elimination of excessive imbalances in the retail market. Anchoring inflationary expectations with the help of targeted inflation had a favourable effect and increased intensity of competition in the retail market also played an important role. The growth in the number of supermarket chains thus started to contribute considerably to damp down inflationary pressures. Over the most of the period monitored inflation was close to 2%, only in 2008 the inflation growth was 3 – 6%. This was caused by an increase in the price of food and energies in the world markets, which had to do both with bad harvest and increased demand for energies in Asia.

3.2. Banks Changed their Sales Strategies

In the given decade banking sector noticed obvious tendencies of a certain shift from a conservative policy keeping to the rule of cautious behaviour to tendency towards a higher rate of speculations and risks. On a practical level it was deepening of credit engagement of banks with moving risks on players who bought bonds with unclear content of their value. Weakened regulatory frames tolerating mortgage credits with low credibility participated to considerable extent in these processes.

Excessive range of mortgage credits issue and growing share of unpaid debts caused that liquidity of a number of banks weakened and the development started to head to critical threshold of bankruptcy. Softening of credit conditions extensively affected deepening of cyclicity in credit segments of the market. The monetary policy adjusted to too low interest rates was primarily accountable for sharp

deviation of mortgage credits issue above the trend line. Growing interest of bank management to compensate lower profitability of credits caused by cheap money policy had similarly negative effect. This compensation meant mainly broader credit issue applying also to lower income population. In reliance with changes in the price of money and the demand, prices of houses grew as well.

T a b l e 3

Interest Rates and House Prices

	2001	2002	2003	2004	2005	2006	2007	2008
Interest rates								
USA	3.7	1.8	1.2	1.6	3.5	5.2	5.3	3.3
Euro area	4.3	3.3	2.3	2.1	2.2	3.1	4.3	4.7
House prices (percentage change from previous year)								
USA	7.7	6.4	6.3	9.6	11.6	7.8	2.5	–
UK	8.1	16.1	15.7	11.9	5.5	6.3	10.9	–
France	7.9	8.3	11.7	15.2	15.3	12.1	6.6	–
Spain	9.5	16.9	20.0	18.3	14.6	10.0	5.5	–
Ireland	8.2	10.7	15.8	11.6	11.8	13.5	1.0	–

Source: OECD (2009).

Several illusions of people played a role in the increase in demand for mortgages. The first one was based on the idea that low and stable inflation would continue even in the ensuing period and so favourable conditions for paying back mortgages were being created. The second illusion was based on the assumption that interest rates would remain at a low level even in long-run perspective. A supportive role in the optimistic environment played also an idea that the state will help, should difficulties arise.

3.3. Failure of Stabilization Policy

Empirical data on economic development in the USA and Europe in 2000 – 2007 showed that the adjustment of stabilization part of economic policy failed in many advanced countries, however, most significantly in the USA. Neither in Europe did the adjustment of the stabilization policy correspond with the growth phase of the business cycle, in which surplus balances are expected, but which were achieved only in a lower number of countries. Thus no favourable environment for a period of lower performance of the economy was created, the period in which a wider manoeuvre room to cover balance deficits from reserve funds is needed. The second offshoot of stabilization policy is represented by a regulatory frame whose task is to filter off risky trades. This frame should prevent a systemic collapse in form of suspending credit activity. Stabilization policy failed even in this field. Secondary mortgage market started to penetrate higher and higher amount of trade with low quality loans, which had a far-reaching impact on

functioning banking sector. Not only did banks stop lending money to each other due to the loss of creditability, but they also froze loans to investment projects. A weakened production potential of the economy could be also seen on a low pace of growth in productivity of labour and wages and it worsened the ability to pay debts. The crises then spread even into the securities market.

Table 4

Overview of Institutions and their Activities Participating in the Current Financial and Economic Crisis

Institution	Activities	Failures	Impacts
Monetary authorities	Monetary policy	Pro-cyclicity	Excessive growth in debts of companies and population
Governmental authorities	Fiscal policy	Pro-cyclic activities	Growth in the state debt
International institutions	Financial stability	Failures in banking evidence	Disruption of financial markets
Banks	Financial services	Failures in risk assessment, social irresponsibility	Liquidity trap, credit freeze
Financial institutions	Audit, bank supervision	Information asymmetry	Moral hazard
Firms, corporations	Firm strategies	Excessive amount of credits	Overinvestment
Population	Investment activities	Disharmony between incomes and accepted loans	Insolvency to repay debts

Source: Table provided by the author.

3.4. Interpretation of Analytical Results

Two views are used for interpretation of the analytical results. The first view is from macroeconomic point of view of a cheap money policy which encouraged credit expansion. This monetary policy resulted in over lending and subsequently in overinvestment in the economy. In a situation when national savings were insufficient, internal imbalance in a form of a gap between investments and savings emerged. This had to be covered by external funds, which created external imbalance on the current account of the balance of payments. Increase in inner and external imbalance was perceived by foreign investors as a threat to the ability to finance the future economic growth. This was a signal for them to transfer their funds to other territories where the potential of economic growth was higher, or to leave their funds in a country, where interest rates were higher and the exchange rate more stable. The fall in financial sources in some economies was one of the important reasons for rising interest rates which ended the upward phase of economic cycle and started a downward phase leading into recession.

The second view, from a microeconomic point of view, is connected with changes in channels of capital flows in global economy. In changed conditions

of the international division of labour the capital has been moved in bigger and bigger extent from advanced countries into segments of manufacturing industry in countries with a lower wage level and bigger competitiveness. Even the banking sector has started to adapt to these changes. This sector has always allocated financial sources into those market segments which show both efficiency and growth potential that usually enables less problematic repayment of the capital borrowed. In bank strategies credits started to be more and more aimed at projects oriented at consumption and investments of the population.

There are three reasons of the altered strategy. Firstly, it is weakening of current and probably also future demand for credits for productive investments in advanced countries because of investment shifts into regions with a higher yield of capital. Secondly, they were using the growth in the demand of population for mortgage and consumer loans connected with a low return risk enabled by the fact, that property can be mortgaged. Thirdly, banks use the situation of low interest rates connected with depreciation of savings of the population to focus their marketing and sales services on advantageousness of provided loans.

4. Economic Policies during Crises

American FED tightened its monetary policy in the beginning of 1928 in response to a rapid growth in prices in securities market which started in 1926. This step was connected with the idea that banks will reduce funding speculations accompanying the boom in securities market and will shift their activities to classical financial intermediating. The increase in discount rate led to contraction in the rendered credit and monetary base. Its consequence was a turn towards a downturn phase of the performance of American economy starting in August 1929, i.e. before Black Friday on American Stock Exchange in October. Monetary development showed that the FED was not flexible enough in its effort to avoid collapse of money supply e.g. by supporting recapitalization of banks or by open market operations (Friedman and Schwartz, 1963). As a result the FED lost control over the monetary development, which led to panic among people, who massively withdrew their deposits and thus made the position of banks even worse.

The monetary system based on the gold standard played a fair role in crisis spreading both within the countries and over borders of individual countries. Destabilization movement was caused predominantly by the growth in the price of gold, which disrupted the balance of internal and external purchasing power of gold and thus led to an increased pressure on reduction in internal prices. Deflationary pressures thus had a key impact on reducing the room for profitability and viability of companies but also on the decline in foreign trade. Persisting of

financial authorities on maintaining the gold standard contributed considerably to the length and depth of the crisis. The practices of the authors of economic policy during the crisis in 2007 – 2009 differed from that of monetary authorities during the Great Depression because they used a dramatic cut in interest rates in order to improve access to loans and thus also liquidity of banks. This technique could be applied since it was not necessary to restrain inflation, as the commencement of recession forces had decreased the price of oil significantly, which enabled replacement of inflationary pressures by deflationary ones.

Differences in the approach of economic authorities to restraining the crisis are obvious even in the budget policy, where in the current crisis the state plays a role of the last resort already in its course. The state tries to avoid panic and run on banks by increasing guarantees on deposits and faces the risk of a systemic impact on functionality of financial services intermediation. However, problematic are efforts of economic authorities to support non-financial companies, particularly automobile industry. It is a measure, which is protectionist and discriminatory not only against other industries. At the same time it establishes a precedent to be followed and to return to interventionist policy. This also leads to artificial increase in competitiveness in international markets.

Responses of economic policies to the economic crisis differ from country to country. Explanation for this can be found not only in differences in the level of macroeconomic imbalance, level of indebtedness of countries, and in the characteristics of impacts of a credit cycle on the health of banks. The second group of aspects, which governments may take into consideration, is whether the proposed measures should lead exclusively to suspension of the slump in economy, or they should help also to effects implemented in a medium – or long-run.

A list of factual intentions which governments incorporated into anti-crisis packages published in the first half of 2009 was aimed mostly at the encouragement of demand, but also of supply. The incentives concern mostly:

- consumption of households by tax adjustments introducing lower social insurance, progressive taxation of physical entities, reduction in VAT for medicine;
- investment processes of both private and public investments through degression of depreciation. Investments will also flow into individual regions particularly with the aim to support labour market, both in form of creating jobs or offering necessary requalification to the unemployed;
- production and export of scrap bonuses, credits and export guarantee;
- activities of banking sector such as by recapitalization of banks, short-term nationalization, support of mergers or withdrawal of bad assets out of banking sector.

In the 1930s such bigger involvement of the state was applied above all after the end of the crisis.

5. Impact on Real Economy

The Great Depression from the beginning of the 1930s represented a recession of economic activity of a substantial extent. Most countries entered recession in 1929 – 1930 and started to recover in 1932 – 1933, in France contraction did not appear till 1932 and lasted to 1935. Slumps in economic performance in the USA, Germany, France, Italy, Japan, Canada, Sweden and Australia exceeded 10%. The highest accumulated loss in production was achieved by the USA and Canada in the amount of –29.4% and –29.7%, respectively.

Investments, which e.g. in the USA fell from the level of about 20% GDP to 5% GDP, suffered the most dramatic slump from the components of production utility. Private consumption fell substantially as well, in current prices by 40%, while owing to deflation it was considerably less in permanent prices (OECD, 2009). A big slump was registered particularly with durable goods.

The rate of unemployment in the USA rose from 3% in 1929 to 25% in 1933. Consumer prices in the USA fell by 30% and international trade by 25%. The economic development in 1929 – 1930 showed a considerable sensitivity of industry to the development in the downward phase of the business cycle. Industrial production in the USA sank by 38%, in Czechoslovakia almost by 40%.

In the economic crisis which started in 2008 almost all countries of the world fell into recession at the beginning of 2009. In the first quarter of 2009 the year-to-year fall in GDP was 4.5% in EU-27, 4.2% in OECD, 6.9% in Germany, 5.9% in Italy, 9.1% in Japan, 4.1% in Great Britain, 2.5% in the USA, 5.4% in Slovakia, 3.4% in the Czech Republic. The only country which experienced growth in the GDP was Poland, which can be explained by a lower participation of this country in the international trade (Eurostat, 2009).

There are data giving evidence about strengthening of recession forces in comparison with the previous quarter. On the demand side of the economy the most dramatic fall in export was by 17.7% in EU-27, by 10.9% in the USA, and even by 36.8% in Japan. Even the major driving force of economic growth concerning investments showed sharp recession. Investments fell by 9.8% in EU-27 and by 14.8% in the USA. As one could expect it was the industry which on the side of supply fell most of all, by 14.7% in EU-27 and confirmed thus a pro-cyclical behaviour, when it usually overtakes the GDP growth in the upward phase and in the downward phase it is the other way round.

Comparison of crisis impacts on real economy during the Great Depression and the crisis started in 2008 signals both similarities and differences. Comparison showed (Eichengreen and O'Rourke, 2009), that the speed of the slump in the GDP and industry was almost the same in the first months after the emergence of the crises, however, it differed in individual countries.

In 2010 the growth rate in the euro area was 1.7% and is projected to be 1.6 and 1.8% in 2011 and 2012, respectively. Countries that had steered clear of large current account deficits, excessive debt, and real estate bubbles in the pre-crisis years have managed to rebound quickly from the global crisis thanks to their highly competitive economies. Germany and Sweden in particular have enjoyed buoyant growth. But countries that built up excessive debt and leverage before the crisis in 2008 are now going through a difficult period of adjustment. Greece, Ireland, and Portugal all had to fall back on financial support from the EU and the IMF. Their near-term growth prospects are clouded, but the support packages now in place include a number of measures designed to cushion the adjustment and restore growth over time.

6. Similarities and Differences in the Analysed Crises

6.1. Differences in the Crises

Empirical evidence proves that the beginning of current financial and economic crisis was influenced primarily by an excessive consumption of inhabitants. This was most apparent in growth of housing expenditures and overall consumption. The supply side of the economy contributed to the crises above all with an oversized capacity of financial sector accompanied by an excessive growth of assets and profits. A very specific feature of contemporary economic crises is that all major types of financial crises concerning development in currency exchange rate, banking sector and value of liabilities of economic subjects had negative effect to the economic recession.

On the other hand, economic development in the pre-crisis period of Great Depression proved that the main moving force setting off the recession was an overinvestment and excessive consumption of goods. The main reason for worsening of the situation in the financial sector, however, was a negative impact of high real interest rate and the fall of real economy, namely gross domestic product and employment. That situation generated a credit crunch and a general uncertainty about the economic outlook. Fall of domestic and foreign demand and consumers prices was playing a key role in protracting and deepening the Great Depression. Similar differences from the situation in the pre-crisis period were during the current crisis registered in the surplus of public budgets and balance of trade, which signalled a lower rate of macroeconomic imbalance and creation of a better background for revival from economic recession.

One of other features of conditions for the emergence of the current crisis was a global economic imbalance. This concerns relations among oil importing

countries, including the USA and most European countries, which started to lack free monetary sources, and oil exporting countries, which were becoming rich fast and thus had a surplus of financial resources. This fact contributed to diminishing the resistance of developed countries to the on-coming financial crisis.

A specific characteristic feature of the financial crisis of this decade was the application of new practices. This concerned an issue of insufficiently transparent financial products, which spread all over the world in the form of bad bonds. Among the differences between the current crisis in comparison with the Great Depression was also a state assistance to low-income mortgage applicants, which, had an impact on the growth of indebtedness of the country.

The list of different conditions of the current crisis should not miss a wider political and economic context. This consists particularly in the advanced level of globalization processes connected with free movement of labour, capital, goods and services across state borders. And it was this area where time discrepancies in the level of development of globalization processes in financial sphere appeared.

On the one hand the level of interconnection and integrity of financial markets was growing steadily, but on the other hand many legislative and regulatory frames have still been created on the level of individual countries. The consequence was information asymmetry between providers and receivers of financial services. Bond providers knew a low value of bonds, while receivers were buying bonds in good faith that these are non-risk securities.

Marked changes in adjustment of the currency and fiscal policies already in the course of the crisis represent another difference from the Great Depression. These changes concerned a substantial reduction in interest rates, application of anti-crisis packages and increased guarantee of population's deposits which played a key role in avoiding panic that would lead to bank runs. The reason for their application was a threat of collapse of banking sector liquidity. In the period of the Great Depression similar bigger state interventions came only after the crisis in the form of the New Deal programme.

6.2. Similarities in the Crises

Comparison of the two economic crises in their pre-crisis periods showed that there were several similarities. First of all it was the fact that both crises were primarily caused by failures in monetary policy, when interest rates in the pre-crisis period were low and left their trend lines. This feature was slightly stronger in the current decade which means that even the monetary policy was a bit more active than the one 80 years ago. Thus it might have caused also a higher level of optimism in credit-gaining effort.

Control functions in managing mostly credit, but also market and currency risks belonged to major weaknesses in both crises. A common feature of both crises was assets over-creditness and overinvestment of assets in the first case mainly of the securities market and of mortgages in the second case. A number of these similarities of both crises is surprising, as if the lesson from the Great Depression had not been sufficient. It happened notwithstanding that in contrast to the previous crisis there were now not only international institutions available, but also high level IT which could have speeded up monitoring and analytical work and even decision-making processes.

There were similarities also in the institutional arrangement of the banking sector. At the time of both crises legislation allowed to interconnect commercial and investment banking. Thus banks faced two risks, credit risk and market risk. Therefore at the time of a financial crisis banks showed losses from overstated and unpaid debts as well as from slumps in securities market. Even though from the above-mentioned reasons universal banking was not allowed in the period after the Great Depression, in the 1980s, however, the legislation was changed to the original state again.

Conclusion

Based on the analysis of causes, course and impacts of the assessed economic crises following calls for shifts in the adjustment of macroeconomic stabilization policies and systems for monitoring, analysing and managing financial risks can be identified:

Resignation on activism in expansion and restrictive monetary and fiscal policy. It is important to replace it by such adjustment that would contribute to the creation of conditions for macroeconomic balance and thus also to reduction of public and private debts. Should public indebtedness continue growing then pressure to the growth in the price of money and thus also costs on debt service might be expected. Problems with debt remittance can't be excluded, since even the state may have liquidity problems which already several countries had to face and when the situation had to be solved with help of international institutions.

Strengthening stability and responsibility for functioning of banking system. The main reason is that banks have only about 10% of own capital at their disposal and other financial sources are borrowed from deposits of population and companies and so their responsibility is extremely high. Therefore it is important to set adequate control mechanisms. It is not only about correcting ways of managing risks in banks, but also in rating institutions, by bank supervision, auditors and top management of banks. As understatement of bank risks was one of the main

causes of financial and economic crises, deepening of their monitoring and improving of the informative ability of bank accounting should be considered as one of the top priorities of preventive measures for the protection of financial stability.

Improvement of procedures of timely indication of market, currency, liquidity and systemic risks with help of an internationally standardized monitoring system. It would be based on an integrated set of indications of financial vulnerability, macroeconomic balance and effects of macroeconomic policy. Composite (aggregate) indicators of financial vulnerability or financial stability might be constructed to complete informative abilities of individual indicators. In case that there will be no trustworthy financial barometer, information asymmetry of economic "players" will deepen and moral hazard may appear. Not only bankers, but also producers, exporters, investors, salesmen and creators of economic policy may be harmed or misinformed.

Promotion of better international cooperation in setting international standards within the financial system. As important fields of cooperation can be considered deposit guarantees, bank recapitalisation, mortgage securitization and solution of relations between banking sector and a shadow sector, which is not under bank supervision. If there were not standardisation of legislations on in the globalization process, then globalization effects enabled by free movement of labour, capital, goods and services might be endangered.

Currency regimes should be more flexible. The reason for this is that big economies should not be tempted to influence them. Thus this would also widen the possibility of adjustment processes in response to incurred shocks, which particularly economies with fixed exchange rate lacked in the current crisis.

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