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# Bad Government as a Reason of Recent Financial Crisis in Europe

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***Abstract:***
*In spite of emphasizing on a market by economic liberalism, most experts believe that market failure caused the deepest global crisis after Great Depression (1929) to happen. Although we cannot ignore the importance to the role of attendance of government to the economy, we believe that sometimes governments are the reason behind the problems in economic situation. Factors like the lack of political integration between European governments and cooperation of national government, the absence of mighty government to make decision and policy and undisciplined financial plans, as well as, loss of proper rules and low, which are occasions of bad government.*

***Key Words***:
*Financial Crisis, Bad Government, European Union*

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## 1. Introduction

Maybe nobody believed that occurrence of price bubble in the housing market in the United States, before 2007, and bursting them, in July 2007, is the origin of the most harmful recession in the world economy after the Great Depression of 1929. The global crisis, which was started from financial market in 2007, was enlarged to real economy, affected the production process, and finally involved the goods and services, labor, and capital markets in the last quarter of 2008. Recent financial crisis caused the world to face a harsh and rapid down fall in production of industries, reduction of international trade, lack of mobility and attract of foreign investment, and debt crisis.

Asian countries, especially South-East Asia always desired to constitute a union with closed and unlimited economic, social, and political relationship among countries within this region, like Europe Union by common currency such as Euro. The bad experience of financial crisis in Europe Union caused to scruple to form and organize a new union in Asia regardless of having the required potentials. East Asia has passed a terrible crisis in the nineties which economists enumerate several reasons to happen in this part of the world. Lack of productive investments of savings, currency value appreciation in the last decade, which undermined export competitiveness, dependence on flight capital for economic growth coupled with lack of proper financial infrastructure to manage huge capital inflow effectively, and the inherent weaknesses of corporate strategies of large and dominant local financial institutions, are causes to occur the crisis in East Asia(Mohamad & Nassir, 2000). Some economic experts focus on this issue financial crisis of East Asia was transmitted between these countries. They have explained which high-powered trade relationship between East Asian countries caused each non-significant and inconsiderable shock, which happens in these countries is transmitted easily with connections of economic channels among countries within this area.(Gong, Lee, & Chen, 2004)

This kind of thinking, with the occurrences of serious financial crisis in Europe has prevented the effort to constitute the Asian Union to organize a new union like European Union with common currency like Euro among themselves. The current crisis of European Union is the most horrific crisis that has happened since 1957 when this union was formed. Most experts believe that recent financial crisis has made difficult for the convergence of European countries. The indebted countries of the union like Greece, Italy, Spain, Ireland, Spain, and Portugal have to refund their debts by economic austerity plans otherwise; we will encounter dark and hopeless perspective for European governments.

Among the results of the financial crisis in Europe was the risk of collapse of Euro unit, instability to the whole of the European financial system as well as the decline in economic growth by 4 percent. At the same, the debts of European government have tripled from 2008 up to now, resulting in the enhancement of European government's deficit at the end of 2009; this deficit was about 9 billion euros. The labor market has also suffered with the increase of unemployment from 7.5 percent in 2008 to 9.9 percent in 2009 and 11.5 percent in 2011. In addition, the region has experience decrease of interest rate from 4.25 percent in 2008 to 1percent in the last of 2009, reduction of exports, the downturn of housing value and bankruptcy of most European banks. Financial indiscipline of members, the lack of regulatory mechanism on operation of European banks and existence of competitive and non-competitive economic together are the most significant reasons which the weak countries of Euro area suffered a severe deficit during several years (Thalassinos, Liapis and Thalassinos, 2011a; 2011b). Then they borrowed continuously and finally; they could not repay them.

In addition, financial crisis has caused a political gap among member countries. In one hand, weak countries of southern Europe believe that hegemonic policy in Germany is the most substantial reason to create the gap between these countries. According to this view, commercial imbalance between members who have a trade surplus like Germany and members who are in a trade deficit situation such as Greece has created the trade deficit among members of Euro zone. Moreover, economic critics explain that Germany has forced members who are debtors to do economic austerity plans as preconditions to borrow and these plans are limitations to achieve the economic growth. On the other hand, Germany claims financial crisis of Europe is a result of prodigality and financial indiscipline of members of European Union and their non-competitive economic, because the governments dominated their economies.

In actuality, financial crisis has eventuated to the defeat for all the members of Euro zone. The feeble members will experience the collapse of value of national money, ungovernable inflation and enhanced foreign debt, which eventually lead to a complete economic bankruptcy. On the other side, the powerful countries, which mainly include western European countries, the crisis will cause them to lose their sales markets and will decline demand for their productions. As a result, they will face impressive unemployment and will lose their economic position in the world.

However, transmission of recent crisis to Europe Union also showed that although the economic interconnectedness has more profits, in economic inappropriate situation, the crisis could have the harmful effects.

Chiefly, when the smaller economy is dependent on large economies and economic unstable of developed countries could worsen the conditions of economies, which have the lower rate of economic growth and even cause the bankruptcy of the economy. Greece, Ireland, Italy, Spain, Portugal, and Cyprus are examples, which can support our statement (Thalassinos *et al.,* 2010).

The significant point that we should bring up, here, is that governments can have considerable effects to reduce the negative effect of economic crises. Nevertheless, it is necessary to remind that sometimes governments, themselves, cause to create fluctuations in crisis. This problem reduces the level of standard of living of residents and lessens the satisfaction of people. The experience of countries of Euro zone is a documentary reason, which displays the incompetence, and inefficiency of their governments, which has caused the deteriorating the situation. As a result, most experts believe that the resent economic crisis has been the crisis of government. Then we can strongly argue that bad government not only able to manage the economic shocks and fluctuations, but also they sometimes act as a catalyzer to worsen an economic process.

Consequently, in Part two, we will review the background of what happen in the financial crisis in Europe and the role the government played in this crisis. Part 3 will offer our finding about the role of bad government in the occurrence the financial crisis in Euro Zone, and eventually in part four we will conclude our discussion of crisis and bad government.

## 2. Background Literature of Recent Financial Crisis

Since after the Great Depression, people said, “we have to make sure this never happens again." Then they had done anything, what was intransitive, to avoid this similar bad economic situation, but the world experienced one in 2007 that created similar situation for people around the world. Ahamed (2009) in his book points to harsh great depression in 1929, the important hint, which is explained by Ahmad, is the mistake of four original bankers’ decisions about the world. He shows that presidents of England, France, and Germany’s central banks also Federal Reserve president the four people responsible to cause the Great Depression. After World War I, the central banks' insistence to use the “Gold Standard System” has caused the monetary irregularity and the great crisis of the twentieth century.

Some crises happen in stock markets (1929), and some of them occur in credit markets (2007). Moreover, sometimes we witness that exchange market and even goods markets experience different crises. These crises can affect one country or a group of countries and maybe the whole of the world. The first crisis started by a collapse in the stock market and second happened with falling into a credit market.(Herring & Wachter, 2003) Show that most financial crises happen since we face bubbles in real estate markets, and the appearance of the bubbles can have different reasons.

Allen and Gale (2009) argue that there was a bubble in real property prices in the USA and European countries, and the most important reason behind this phenomenon was the loose monetary policy by the Federal Reserve and global imbalances.

Occurrence the crisis in financial markets of USA is being referred to the early twenty-first century[1].In addition; China could conquer the most goods markets of USA. China could, for the first time, decline American demand for internal production. In other words, the consumption of United States from goods, which were produced in USA, had decreased while its import had gone up. This problem caused bad situation for growth process. Moreover, 11 September happened in 2001. Which damaged economic power of USA and had negative effects on financial markets? This caused capital flight for the greatest economy of the world. Morck, Deniz Yavuz, and Yeung (2011) believe the United States is experiencing a sub-prime mortgage crisis, which is creating a deep economic winter.

By studying the case of European countries that is a member of EU, it seems that the most important problems of this zone during the financial crisis and after that even up to now, has been the lack of political integration between the West and East Europe countries. Clearly, Euro zone crisis in 2007 has boosted the significance of presence the powerful government to create collaboration between the West and East Europe. Unfortunately, the manifest problem that the Europe Union suffers from it, according to theory of Benink and Schmidt (2004), is the absence of political integration.

Most economists claim that euro is the origin root of the financial crisis in Europe. In their view, this problem started when the plan of a money union was done without a financial merger. It means; it was necessary that with money union established an organization which proctored on providing budget system tile all the members of the union were dedicating a constant ratio of domestic gross production to their budget.(Hall, 2012) Moreover, incident of financial crisis changed the market failure to one of the hottest topics in economies. Páramo (2009) shows that, information asymmetries as type of market failure, has raised inefficiency of securitization markets and behavior of investors, rating agencies, intermediaries, and originators, which has had a direct effect on financial markets to face the crisis.

Here, we face so many questions, which we have to find an appropriate answer to prevent global economy from future crisis, like what are the lessons learned from the current crisis. What are the important reasons to start the crisis and how can we confront prospective problems? Alternatively, is there a need for government to control market failure, which it seems, is one of the roots of occurrence of financial crisis?

Hoshi and Kashyap (2008) simulated the Troubled Asset Relief Program (TARP) model of the United States for Japanese financial crisis and illustrated that government must navigate the financial markets during the crisis via equity injection. In addition, Bebchuk emphasizes that fluctuation situation can lead the financial markets into crisis, we have to consider a government-funded asset purchase program.(Bebchuk & Spamann, 2009)

This global financial crisis corroborated that accretion and affiliation of the economy are two points, which are needed for a regulative system and constant international financial framework. Ozkan (2011) proves that global governance can be useful for the recovery of the economy after the recent crisis. He describes an effective, defined, and legitimate global governance of G-20 to improve the worse economic situation of the world. Chua emphasizes that to recover the global crisis in 2007; we have to reign diplomacy efforts,(Chua & Pang, 2012). Benink and Schmidt (2004) describe what can play an effective role in critical economic conditions in the new world, which the global economy is integrated, is political integration. To this end, the best option is still national governments. In addition, to create accretion between the members of Euro Union, the tool, which we need, is diplomacy (Hiebert, 2005) . Now, we believe when a prosperous diplomacy happens between these countries, initially all of them are able to organize a prosperous political and economic communication with each other.

As a result, with studying the literature of government support in crisis, we will show that government assistance will guarantee the reform of financial market when they face the crisis. Finally, even government can hold up outbreak of financial crisis, but government should have special character, which we will refer to them in the future. Otherwise, government can be the reason to create fluctuation; in so fair, some economists believe the recent financial crisis is the government crisis. It can be said that bad government lead to bad situation in societies.

## 3. Finding

Expanse of the number of countries' encounter risk of bankruptcy in Europe Union, and enhancement of famine and hungry in Africa and some part of Asia confirmed, after four years, world economic situation still feels the danger of harmful effect of recent crisis. Moreover, countries have not been able to reform completely their situation. Even according to the annual report of UN and DESA in 2012, the world has experienced the weakened economic situation.("World Economic Situation and Prospects 2013" 2013)

Debt crisis, bankruptcy of some Europe countries and high rate of unemployment are some problems, which the developed countries face them. Weakening the power of Euro and lack of fiscal discipline of European government are two factors, which help financial crisis to be changed debt crisis and the high risk of bankruptcy for some governments, while the rate of unemployment also shows in Europe the number of people who are losing their jobs will be raised. (Table 1)

Debt crisis has entailed the rate of economic growth was been negligible and Europe governments have so many problems to solve them and improve their situation after recession(Galooyek & Noor, 2013). The interesting point is the imperfect condition to form the Europe Union has been transmitting the crisis among countries, which are members of Euro area. The member of Europe Union whose their process is done by currency, not Euro, are less vulnerable that Euro zone. This acknowledges Euro is one of the variables to make economic fluctuations.

Over four years of financial crisis, which started from USA and gradually changed into the global crisis, the world has not been able yet to return to the conditions before this recession so that it seems, some countries around the world have experimented the awful situation than before. Maybe, we should say that the Europe Union's countries have had the most horrible economic status. The low rate of the growth, the high number of people, who lose their job every day, and labor unions' protest were problems that countries like Greece, Cyprus, Ireland, Spain, and Italy were struggling with them. Even if the Euro Union had not supported them eventually were falling into the bankruptcy trap, and it was possible the Euro was disappeared. In short, Europe governments now have been confronted two major problems; low rate of economic growth and debt crisis.

Although the downturn in Europe has dramatically affected the labor market and increased the number people who lost their job position to 5.4 million duration between March 2008 and May 2009 (Hijman, 2009), it has been a positive opportunity for students and scholars of political economic filed in Europe. Based on this, economic experts have represented numerous reasons to happen the recent financial crisis, if we want to conclude, we should mention the financial crisis is due to fail the foreign and domestic decision.

Pauly (2009) and Schneider & Kirchgässner (2009) indicate, reluctance of government to develop coordinating policy between a domestic and foreign courses is a root to occurrence the financial crisis in Europe. Begg (2009) argues that deregulation and failure of regulation are factors, which caused the global crisis in financial markets.

The important point in studying of financial crisis in 2007 is even the economics have not found any convincing answer why the current financial crisis happened. Although, in duration of the new crisis, which started from advanced countries like the United States, governments had to inject liquidity to financial organizations and systems and in spite of some governments and nations to prevent bankruptcy, one definitive solution has not been found yet and economies, which have confronted downturn and bankruptcy, especially, some European countries are vulnerable and fragile.

Pauly (2008) believes albeit integrated financial and capital markets in Europe have deeply prospered. Financial crisis by 2008 showed they have not been able to contrast with crisis and protect economic stagnation and collapse into insolvency and failure. Then we cannot ignore forming global governance with effective and undeniable instrument like free, integrated, efficient and resilient financial market can be an engine of economic growth when in Europe, these markets are matched with what European named them as complex politics. In better word, we need a responsible power parallel by markets. As a result, according to the theory of Akerlof and Shiller (2010) we accept that rebellious mind of people as the animal spirit was a reason to fall the value of Dow Jones in the United States, FTSE100 in England, CAC40 in France, and DAX in Germany. In addition, the appearance of government, as the kind of parents to bring up and train of children is required to control and manage the economic situation within a society or government is as an essential terrible. Nevertheless, bad government not only cannot reform the critical situation, but also it can worsen the condition even can be a reason to bankruptcy of a country.

Davidoff and Zaring (2009), by emphasizing on theory of Kindleberger and Aliber (2000), illustrates sometimes the response of government could push the circumstance of economy to downturn and even bankruptcy. Afterwards, we can mention what governments have done to restore the economy of Europe, although was creatively, in most times they have been executed imperfectly because of low confidence of government. Next what they have done to decrease the effect of crisis was hastily, as well as was good and enough only in short time. This kind of policymaking could not guarantee the long-run improvement in European societies. In addition, the unbounded but complex communications in a new world have been causing the world move to moral hazard which government has had a major contribution to violation of ethics. It means that, we live in the world which free riding on government is a custom even in societies are experiencing the integrity process, and they have to be committed to ethics. For example, cheating of government of Greece from 2002, when joined to Europe Union, to offer the data and macroeconomic information to global institutions entailed decreasing the risk of lending from powerful economies and financial international organizations to this country. However, by deploying the financial crisis from the United States to Europe Union and inability of Greece's government to refund the debts, Greeks tried the terrible economic situation up to bankruptcy.

Finally, prevalence of Thatcherism ideology in Europe in eighties recognized the market without the intervention of government as an only engine of development in societies, as a result the role of government gradually diminished in economy. Large scale of privatization of most economic sectors and deregulation which done in most advanced countries.Benáček (1993) believes what accomplished by government as privatization and deregulation was because of being unable to government. Benáček (1993) indicates the market is a kind of public good, as well as Keech, Munger and Simon (2012), explain that the market failure will happen cause government failure. It means when a government is not able to amend the structure of market, we will face market failure. Recognizing of market as state good displays to construct it, we need infrastructures, rules and huge investment, which a government could only provide them. In other words, market is a special public good that has much authority to affect in economy. If we accept the market is a public good, free market without any intervention of government, and irregular liberalization will be sung of inability of government.

## 4. Conclusion

We can strongly say the first years of twentieth-century people of the world experienced too agonizing and frightful situation when happening the Great Depression was a tragedy for these years. Between 1930 and 1936, the rate of unemployment fell into 25percent. The financial crisis in these years started from the United States and affected whole the world for one decade. Although Ahamed (2009) believes that this crisis befell because of making mistake decision by the presidents of central bank of England, France, Reichsbank of Germany, and Federal Reserve of New York, maybe, investigating of the reasons of occurring the financial crisis in these years is not more important versus failure to provide the appropriate solution to eradicate the downturn. Since lack of ability to recover, the economic situation in during the years between 1929 and 1936 caused the World War II was considered as the only solution to reform the recession condition by politicians. The result of was death of more than 50 million people in worldwide. This issue was more irritating than occurrence the crisis in 1929. That is why, repeating the financial crisis in 2007 the world entailed fear and anxious to be pulled into other wars.

Moreover, financial crisis in 2007 in developed countries illustrates, in spite of what is being claimed. Development is not a reason for being protected of economic fluctuations and tensions, especially when in definition of development the prevailing view is the economic growth. The increase of the number of unemployment with decrease of national production in the United States in during of 2007 and 2009 is a strong proof on this asseveration. Transmission of recent crisis to Europe Union also showed that although the economic interconnectedness has more profits, in economic inappropriate situation, the crisis could have the harmful effects. Chiefly, in situation, which the smaller economy is dependent on large economies and unstable economy of developed countries, can worsen the conditions of economies, which have the lower rate of economic growth and even cause the bankruptcy of the economy. Greece, Ireland, Italy, Spain, Portugal, and Cyprus are examples, which can approve our statement.

Keynes in his book, “The General Theory of Employment, Interest, and Money” has offered his theory based on the prominent role of government in a strong capitalism economy. The thinking of appearance of government, as a necessary bad, formed in whole the world. Keynes clarifies how a strong and qualified government can make appropriate policy and even borrow to cost in economic stagnation to hire the force labors that is unemployment (Keynes, 2006). Although the prescription of Keynes was never completely executed in during the crisis, from the end 1940s, the solution of Keynes was performed for all the countries of the world. Then by finishing the Second World War, governments, as proper manager to reconstruct and plan of society’s development, could reduce the rate of unemployment. As a result, the appearance of government to manage the economy is one of the undeniable factors in business cycles. Though Thatcherism and Reganism thinking at first of eighties was a reason to forget this factor, many experts believe these issues were the beginning of the numerous economic shocks like financial crisis in 2007.

The significant point that we should bring up, here, is that governments can have considerable effects to decline the negative effect of economic crises. Nevertheless, it is necessary to remind that sometimes governments, themselves, cause to create fluctuations in crisis. The experience of countries of Euro zone is a documentary reason that displays the incompetence and inefficiency of European government has caused of deteriorating the situation. As a result, most experts believe that resent economic crisis has been the crisis of government. In better word, bad government is one reason to deteriorate also move to bankruptcy. We should clarify that the lack of confidence in governmental planning and then offering the short time and hastily decision and policies are factors to approve the bad government is on reason of recent financial crisis in European Union. In addition, absence of morality of governments to respect the rules of the process of integration, privatization and deregulation, because of inability of government in managing of government not to support the private property, and weakness of government to do responsibilities to create and construct the market as public goods are causes to define the bad government to worsen the economic situation of Europe.

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