

a "beggar-thy-neighbor" policy), its domestic expenditure has to increase. Since neither private consumption expenditure nor private investment are showing any signs of a recovery (they would recover once the economy begins to recover), the increased spending will have to come from the government, and, in the absence of taxes upon the rich, will have to be financed by a fiscal deficit (taxes on the poor nullify the expansionary effects of government spending). Curtailing the fiscal deficit, and that too via cuts in expenditures for the poor, will therefore aggravate the recession in the US, and hence the world economy.

Duties of Care in Finance

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Financial crises in the 19th and early 20th centuries were followed by plugging of loopholes in the system or checking the practices which apparently caused the crises. One can conclude that the crises were followed by reforms in the financial system. A prominent example would be, for 50 years after the Great Depression of the 1930s, the 'Money Power' was held to account by the countervailing power of the government. At the heart of the political check was America's Glass-Steagall Act of 1933. Glass-Steagall Act aimed to prevent commercial banks from gambling with their depositor's money, by mandating the institutional separation of retail and investment banking. This cautious approach to banking was later called the 'repressed financial system', by

economists. The act ensured that retail banks fulfilled the necessary function of the financial intermediation without taking major risks, while the government kept aggregate demand high to maintain full-employment level of investment. There was a fundamental shift in the response of the system to financial crises after 1980s. Plugging of loopholes or reforms did not follow financial crises that happened after 1980s. 'Money Power' struck back. There was a demand for more free hand and loosening of controls on financial systems, this demand was aided and abetted by a group of economists. The policy makers opted in favor of this demand. The Big Bang of 1986 in London ended the separation of banking functions in Britain. This major policy shift in Britain fuelled the demand for similar policy shift in other countries, as this allowed the banks to increase their profits substantially. After prolonged lobbying by the financial services industry, US president Bill Clinton repealed the Glass-Steagall in 1999. From that point on, commercial and investment banks could merge and the composite entities were authorized to provide a full range of services, including underwriting and other trading activities.

The merging of the retail, investment and commercial banks has brought forth new set of problems. The retail banking function of banks is fairly stable and involves very low risks compared to the investment banking function. The customers of the two functions also have very different profiles and expectations from the bank. Hence the combining of these functions is definitely not benefiting the retail banking customer, however it exposes them to a far bigger risk emanating from the speculative activity of the investment bankers. Retail

customers have neither asked for nor bargained for those risks. Also, they do not profit from these risks.

Moreover, in the 1970s, post the Nixon shock, Bretton Woods system was severely dented. This weakening of international financial arrangement, laid the foundation of the financial systems to run with a relative lack of regulation. The bankers became increasingly profit centric and started to take greater risks. The opening of international capital markets since the collapse of the Bretton Woods system led to a series of financial crises. There is, however, a common thread between the four major economic crisis since the 70's; they were all preceded by over optimism & that there was a boom followed by a bust. A major part in this boom & bust was played by the banking sector.

As a consequence of the major economic crises, many of the banks went bust. The going bust of banks has been supported repeatedly by the governments. The governments bailed out the banks with large infusion of funds. This support to the banks has been at the cost of tax payers' money. The rescue by the governments is aimed at protecting the retail customers but it actually supports the speculative excesses of the investment arm of the commercial banks. This actually resulted in creation of a system in which there was an extreme moral hazard operating for the benefit of the imprudent financial system. The financial rescue by large scale infusion of public funds has a toxic effect on the economies for a fairly long period with interest rates and inflation rates becoming volatile.

There is a greater need for trust, integrity and morality in the working of commercial

establishments. However, we cannot rely upon the institutions themselves to accomplish this task. Self-regulation is often subject to conflicts of interest between their regulatory responsibilities and their business objectives; self-regulatory role lacks transparency and encourages anti-competitive practices.

The 'invisible hand' does not seem to effectively prevent the run-away greed of financial sector from rocking the boat of the financial system. The recurrence of economic crises in last few decades has illustrated that the 'goodness' of commercial establishments can't be relied upon, particularly in matters concerning interests of public at large.

Governments by the way of public policy are required to play a part in delivering a more professional financial system. Governments can effectively ensure this with appropriate policy measures, regulations and legislations. Integrity can be ensured in the financial system by an appropriate framework which would require ethical standards, management of resources, preventive and reactive capabilities. In order to avoid and tide over the financial crisis, States must restructure the banking system by decoupling their risky and non-risky businesses.

The 'Occupy Wall Street' protests in the US further testify the points made in this article. An average citizen should not suffer because the bankers are taking excessive risks to increase their profits. A pressure group is being formed in the bastions of 'free market', which is demanding a 'control' on the functioning of financial systems. There is a need for institutional mechanism to ensure morality and selfless thinking in functioning of corporations and banks.

One hopes that with the pressure of public opinion this will culminate in introduction of

framework to protect the masses from the financial crises that are perpetuated by greed in absence of adequate statutory and institutional controls on the functioning of the financial institutions.

References:

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The rise and fall of Dubai

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In his book "Manias, Panics and Crashes: A History of Financial Crisis", Charles P. Kindleberger provides an extensive historical account of financial crises analyzed within Minsky's framework. It starts from an autonomous shock to the economic system that alters profit opportunities; the shock can either be the outbreak of war or a bumper crop or a technological advancement or an oil shock, which creates a feeling of buoyancy and leads to a reordering of investment priorities. Consequently, there is an investment boom which may result in 'euphoria' and 'overtrading' i.e, positive (and even outlandish) expectations driving up future prices, followed by more investors entering the market to speculate and earn profits. But the boom may subside by itself

when expectations of its subsidence are caused by the inability of a few investors to repay, which sets in motion a stampede for liquidity. This rush back into money triggers panic, seizure of credit and eventually crisis.

Dubai exemplifies a similar boom-bust phenomenon. The economy was steered by the speculative excess and over accumulation of the boom, which was the outcome of the growth strategy followed by its ruler Sheikh Mohammed bin Rashid-al-Maktoum. The objective behind such a strategy was to transform oil-poor Dubai from an Arab backwater into a global city, so that by the early years of this century, it had become a global hub: the largest international financial centre between Singapore and Europe. But with the current financial crisis, the ensuing contraction in aggregate demand all over the world has led to an inevitable crash that was followed in Dubai. This became clear by the sudden announcement of the state-owned conglomerate, Dubai World, on 25 November, 2009 that it would suspend payments on its \$26 billion debt- these loans involved payments to bondholders of the world's biggest sukuk or Islamic bond issue. It is the presence of this instrument that has thrown serious doubts on the Islamic financial system, particularly, when it was believed that this segment was relatively unaffected by the ongoing crisis.

Dubai is one of seven small states that make up the United Arab Emirates (UAE), and in terms of the size of its economy, it is second to Abu Dhabi (which has most of the oil reserves). Although the economy of Dubai was originally built with the might of oil, but with a significant decline in its oil reserves, revenues from this sector currently account for less than 6% of its