The Great Recession

ANTHONY MANIA

BMBA 9459: ECONOMICS FOR MANAGERS

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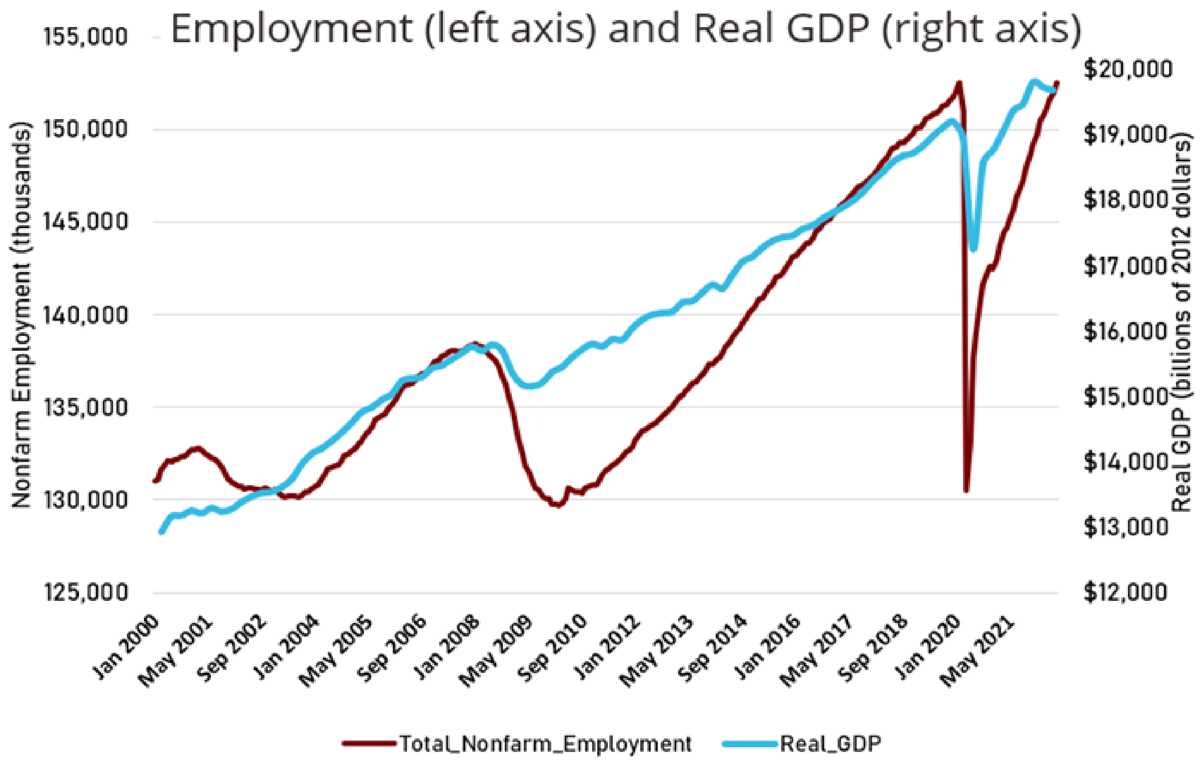
Introduction to the Time Period

- **Time Period:** December 2007 to June 2009
- The longest and most severe U.S. recession since the Great Depression.
- **Outcome**:
  - GDP fell by over 4.3%
  - Unemployment peaked at 10%
  - Stock market lost nearly 50% of its value at the trough
  - Inflation initially dropped sharply, and later surged due to government stimulus

What led to this Recession?

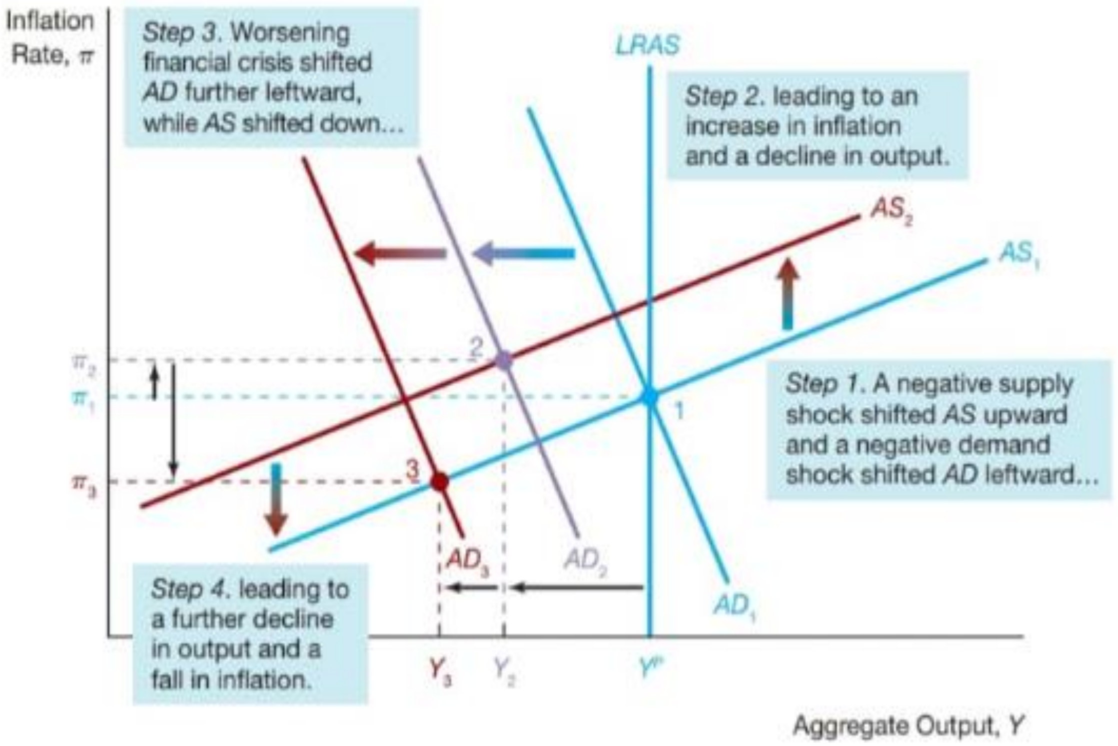
- Burst of the U.S. housing bubble
  - Collapse of Subprime mortgages led to a financial crisis
  - When borrowers defaulted, it set off a chain reaction across financial markets
- Lehman Brothers bankruptcy in Sept. 2008 escalated global panic
- Credit markets froze, affecting businesses and consumers

Real GDP and Employment Trend



Economic Concept 1 – Supply & Demand

- Housing market saw a shift in supply while demand as defaults increased
- Demand for housing fell as prices declined, worsening foreclosures
- Resulted in lower equilibrium prices and quantity in housing markets

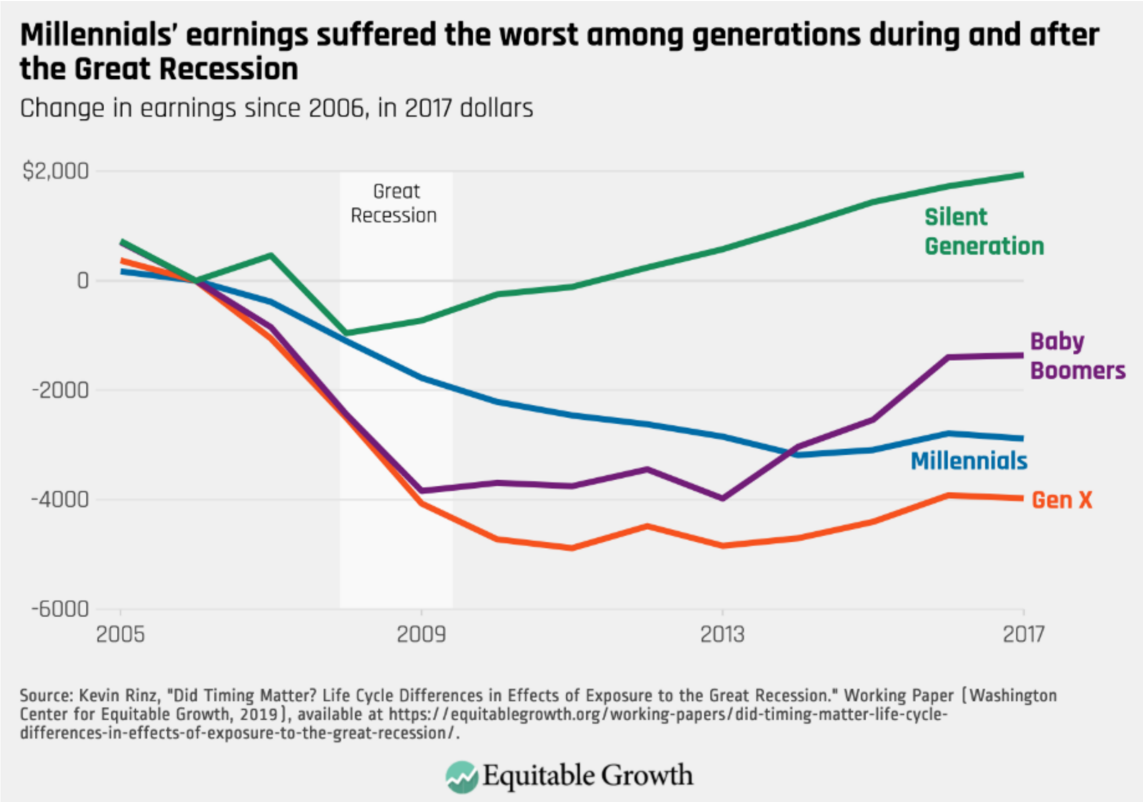


Economic Concept 2 – Principal-Agent Problem

- Mortgage brokers approved risky loans for commissions (agents)
- Investors (principals) bore risk through MBSs they didn't fully understand
- Asymmetric information & moral hazard worsened systemic risk
- Caused a misalignment between risk takers and risk bearers

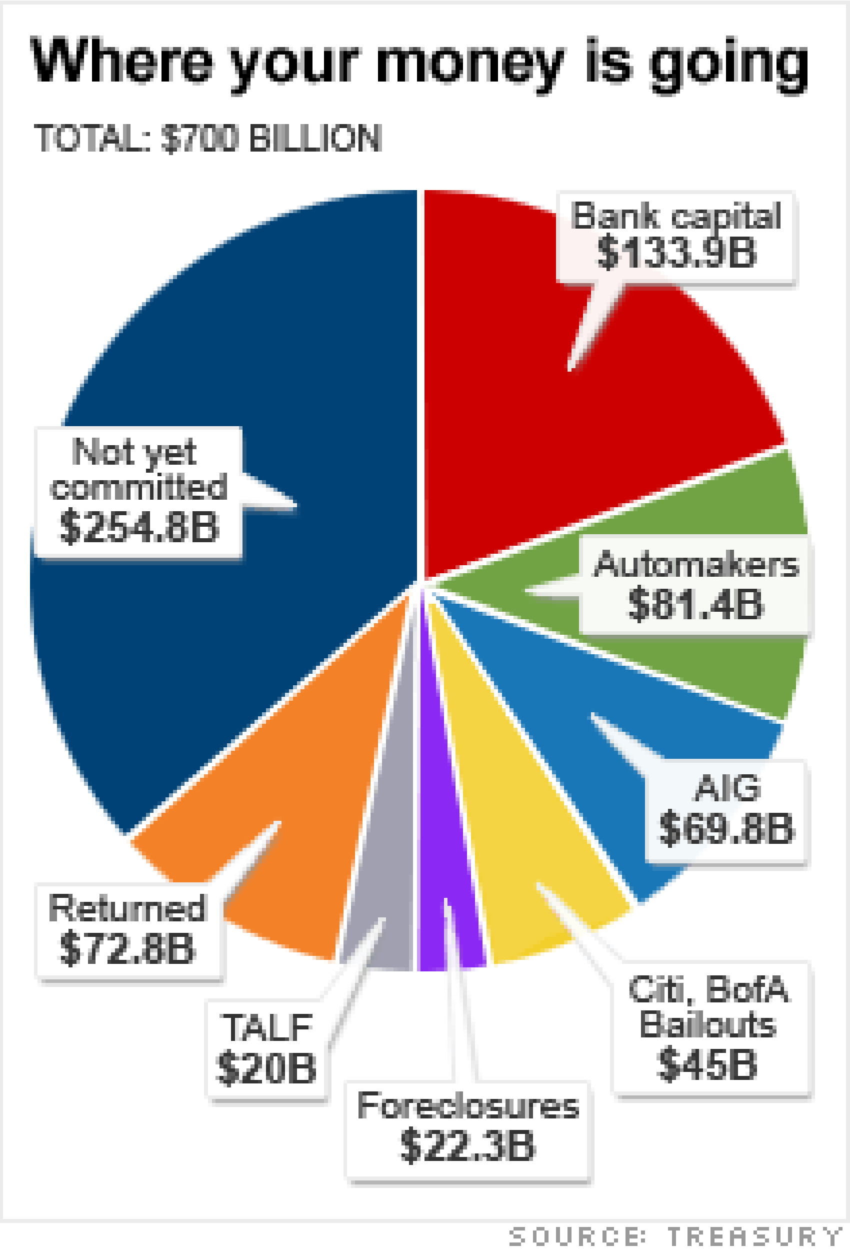
Impact on Specific Groups

- Low-income and minority homeowners hit hardest by foreclosures
- Middle class lost significant wealth through housing and 401(k)s
- Young workers faced high unemployment
- 8.8 million jobs lost; poverty rate rose to 15%



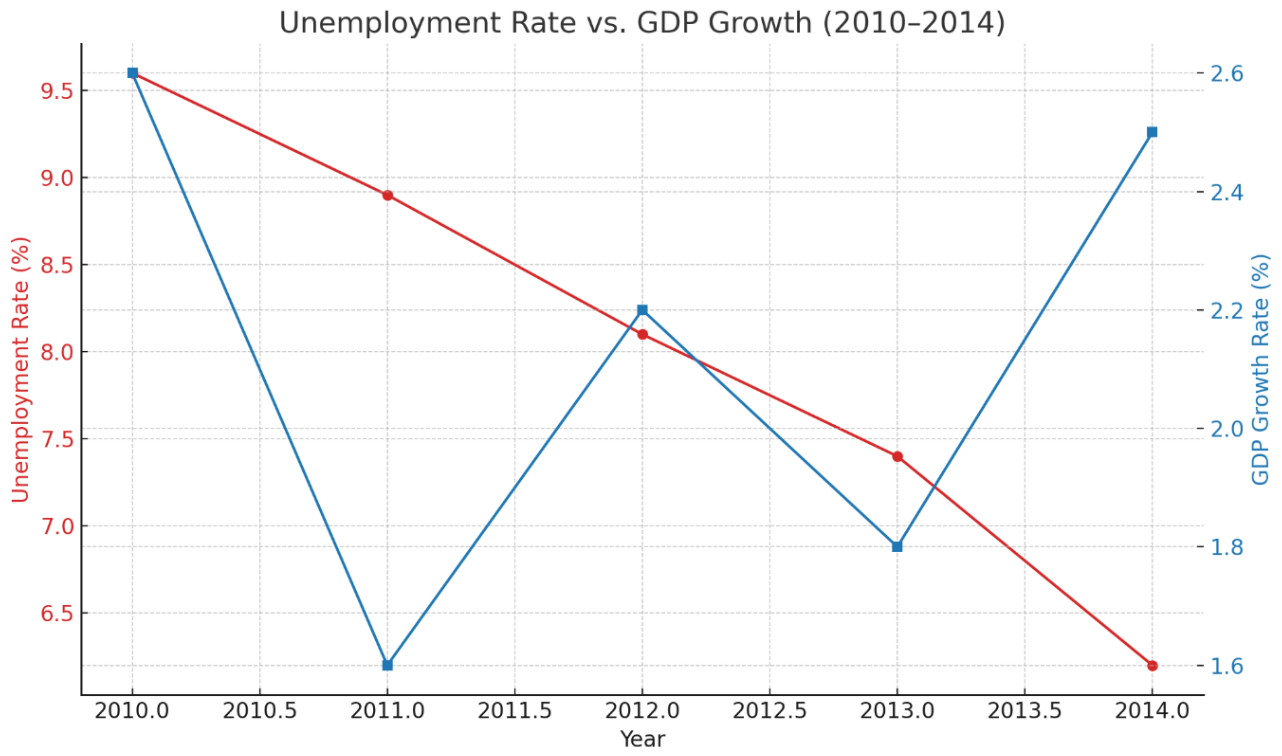
Government Response

- TARP: Troubled Asset Relief Program (700B bailout for banks)
- ARRA: American Recovery and Reinvestment Act ($831B stimulus)
- Federal Reserve: Slashed interest rates to near 0%, began Quantitative Easing
- FDIC increased insurance limits to stabilize confidence



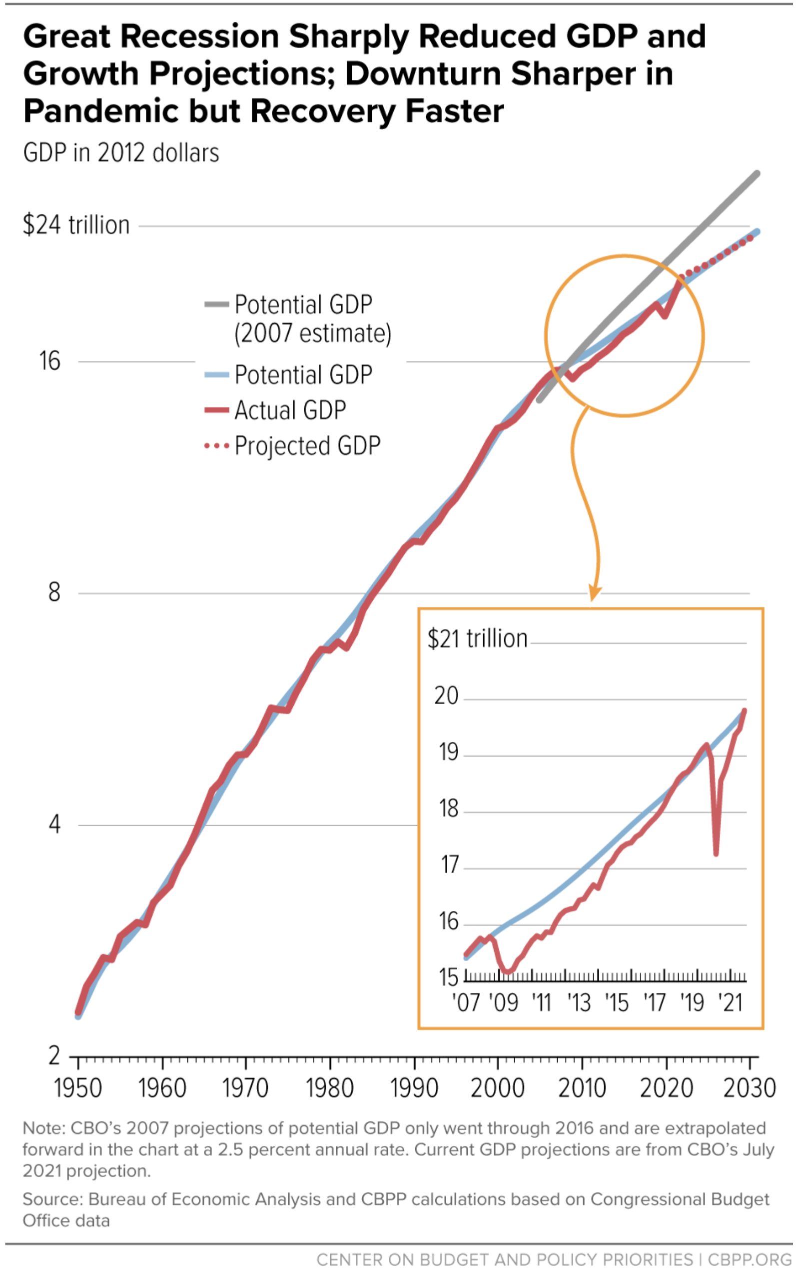
Was the Response Effective?

- Mixed views, but consensus is stimulus softened the blow
- Unemployment decreased steadily post-2010
- Critics argue response favored banks over homeowners



Recovery

- Slow recovery began in 2009; GDP recovered by 2011
- Full employment not achieved until 2016
- Housing prices took nearly a decade to rebound
- Market confidence and spending gradually restored



Policy Recommendation 1

- Implement stricter lending standards BEFORE crisis
- Use early-warning systems to detect asset bubbles
- Apply Dodd-Frank-like regulations to ensure transparency
- Economic Concept: Prevent adverse selection in credit markets

Policy Recommendation 2

- Provide direct assistance to homeowners, not just banks
- Expand public goods: housing counseling, legal aid
- Better allocate stimulus toward local/state governments for employment
- Economic Concept: Government provision of public goods and externality correction

Conclusion

- The Great Recession shows how financial market failures can ripple through the entire economy.
- Applying concepts like supply & demand and the principal-agent problem helps explain its severity.
- Proactive regulation and direct aid to affected populations could enhance resilience.

THANK YOU

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