International Research Journal of Management and Commerce
ISSN: (2348-9766)
Impact Factor- 5.564, Volume 4, Issue 7, July 2017
Website- www.aarf.asia, **Email** : editor@aarf.asia , editoraarf@gmail.com

ECONOMIC DEPRESSION: AN ECONOMIC RECESSION AND DECLINING OF NATIONAL INCOME

Dr. Amit Kumar Khare
Ph.D, MBA, Univerity of Lucknow, Lucknow,
Associate Professor Rameshwaram Institute of Technology and Management,

ABSTRACT

In economics, a depression is a sustained, long-term downturn in economic activity in one or more economies. It is a more severe economic downturn than a recession, which is a slowdown in economic activity over the course of a normal business cycle. Characteristics of an Economic Depression. An example of an economic depression is a negative growth in the Gross Domestic Product (GDP), the measurement of national income and output for the economy. A recession is when the economy declines significantly for at least six months. That means there's a drop in the following five economic indicators: real GDP, income, employment, manufacturing and retail sales. The last century economic depression was the Great Depression of 1929 which lasted ten years and forced millions into unemployment, homelessness, and near-starvation while factories shuttered due to declining orders. Economic depression is a big decline in buying, production and selling in a country that lasts for several years. Recession is when the GDP growth rate is negative for two consecutive quarters or more. Economic Depression is a more severe economic downturn than a recession, which is a slowdown in economic activity over the course of a normal business cycle. Despite the often-applied term cycles, these fluctuations in economic activity do not exhibit uniform or predictable periodicity. Related but distinct concepts include inflation, which is a market-determined decline in the value of the currency in terms of goods and services (related to its purchasing power). Altering the face value of a currency without reducing its exchange rate is a redenomination, not a devaluation or revaluation. Governments usually respond to recessions by adopting expansionary macroeconomic *policies, such as increasing money supply, increasing government spending and decreasing taxation. A central bank maintains a fixed value of its currency by standing ready to buy or sell foreign currency with its own currency at a stated rate; a devaluation is a change in this stated rate that renders the foreign currency more expensive in terms of the home currency. The opposite of devaluation, a change in the fixed rate making the foreign currency less expensive, is called a revaluation. Macroeconomic indicators such as GDP (gross domestic product), investment spending, capacity utilization, household income, business profits, and inflation fall, while bankruptcies NPA and the unemployment rate rise. In the United Kingdom, it is defined as a negative economic growth for two consecutive quarters. Recessions generally occur when there is a widespread drop in spending (an adverse demand shock). Altering the face value of a currency without reducing its exchange rate is a redenomination, not a devaluation or revaluation. The problem of NPAs requires sober analysis. It has to be understood that unlike in the US where the sub-prime mortgage crisis of 2007-08 - NPA under a different name - brought the big banks down and forced the US Federal Reserve to put in place a humongous bail-out package, in the Indian context the banks have not broken under the burden of NPAs.*

KEYWORDS: Macroeconomics, Stagflation, Recession, Devaluation, Deflation, Economic Crisis, Business Economic Cycle etc.

INTRODUCTION

A depression is an unusual and extreme form of recession. Depressions are characterized by their length, by abnormally large increases in unemployment, falls in the availability of credit (often due to some form of banking or financial crisis), shrinking output as buyers dry up and suppliers cut back on production and investment, large number of bankruptcies including sovereign debt defaults, significantly reduced amounts of trade and commerce (especially international trade), as well as highly volatile relative currency value fluctuations (often due to currency devaluations). Price deflation, financial crises and bank failures are also common elements of a depression that do not normally occur during a recession. In economics, a recession is a business cycle contraction which results in a general slowdown in economic activity. Macroeconomic indicators such as GDP (gross domestic product), investment spending, capacity utilization, household income, business profits, and inflation fall, while bankruptcies NPA and the unemployment rate rise. In the United Kingdom, it is defined as a negative economic growth for two consecutive quarters. Recessions generally occur when there is a widespread drop in spending (an adverse demand shock). This may be triggered by various events, such as a financial crisis, an external trade shock, an adverse supply shock or the bursting of an economic bubble. Governments usually respond to recessions by adopting expansionary macroeconomic policies, such as increasing money supply, increasing government spending and decreasing taxation. A central bank maintains a fixed value of its currency by standing ready to buy or sell foreign currency with its own currency at a stated rate; a devaluation is a change in this stated rate that renders the foreign currency more expensive in terms of the home currency. The opposite of devaluation, a change in the fixed rate making the foreign currency less expensive, is called a revaluation. Related but distinct concepts include inflation, which is a market-determined decline in the value of the currency in terms of goods and services (related to its purchasing power). Altering the face value of a currency without reducing its exchange rate is a redenomination, not a devaluation or revaluation. A bank failure occurs when a bank is unable to meet its obligations to its depositors or other creditors because it has become insolvent or too illiquid to meet its liabilities.

OBJECTIVE

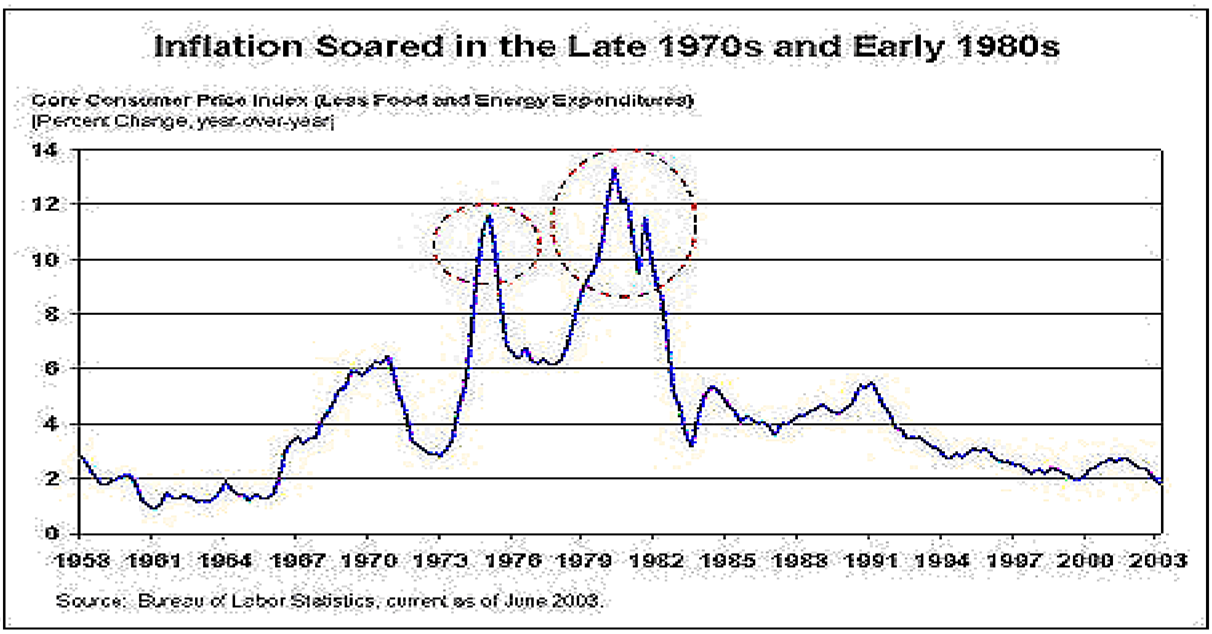
- To analyze the growth and decline of world market economy.
- To access the factors involved depression and in declining of GDP & local market.
- To identify the failure of macroeconomic crisis.
- To analyze the cause of economic depression & NPA.

MACROECONOMICS

Macroeconomists study aggregated indicators such as GDP, unemployment rates, national income, price indices, and the interrelations among the different sectors of the economy to better understand how the whole economy functions. Macroeconomists develop models that explain the relationship between such factors as national income, output, consumption, unemployment, inflation, savings, investment, international trade and international finance. While macroeconomics is a broad field of study, there are two areas of research that are emblematic of the discipline: the attempt to understand the causes and consequences of short-run fluctuations in national income (the business cycle), and the attempt to understand the determinants of long-run economic growth (increases in national income). Macroeconomic models and their forecasts are used by governments to assist in the development and evaluation of economic policy. A bank failure occurs when a bank is unable to meet its obligations to its depositors or other creditors because it has become insolvent or too illiquid to meet its liabilities. More specifically, a bank usually fails economically when the market value of its assets declines to a value that is less than the market value of its liabilities. They advocated government intervention and socialism, respectively, as the solution. This work did not generate interest among classical economists, though under consumption theory developed as a heterodox branch in economics.

STAGFLATION

Stagflation is an economic cycle in which there is a high rate of both inflation and stagnation. Inflation occurs when the general level of prices in an economy increases. Stagnation occurs when the production of goods and services in an economy slows down or even starts to decline.



DEVALUATION

In modern monetary policy, devaluation is an official lowering of the value of a country's currency within a fixed exchange rate system, by which the monetary authority formally sets a new fixed rate with respect to a foreign reference currency or currency basket. In contrast, depreciation is a decrease in a currency's value (relative to other major currency benchmarks) due to market forces under a floating exchange rate, not government or central bank policy actions. A central bank maintains a fixed value of its currency by standing ready to buy or sell foreign currency with its own currency at a stated rate; devaluation is a change in this stated rate that renders the foreign currency more expensive in terms of the home currency. The opposite of devaluation, a change in the fixed rate making the foreign currency less expensive, is called a revaluation. Related but distinct concepts include inflation, which is a market-determined decline in the value of the currency in terms of goods and services (related to its purchasing power). Altering the face value of a currency without reducing its exchange rate is a redenomination, not a devaluation or revaluation.

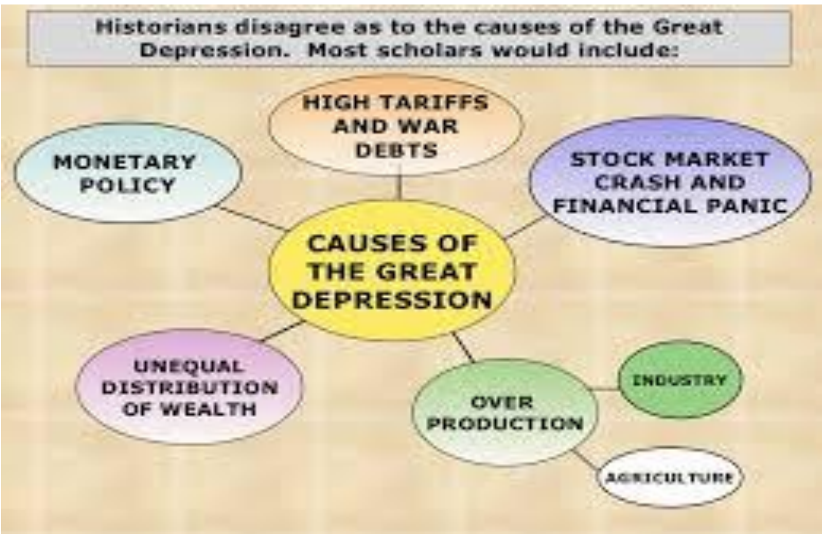
DEFLATION

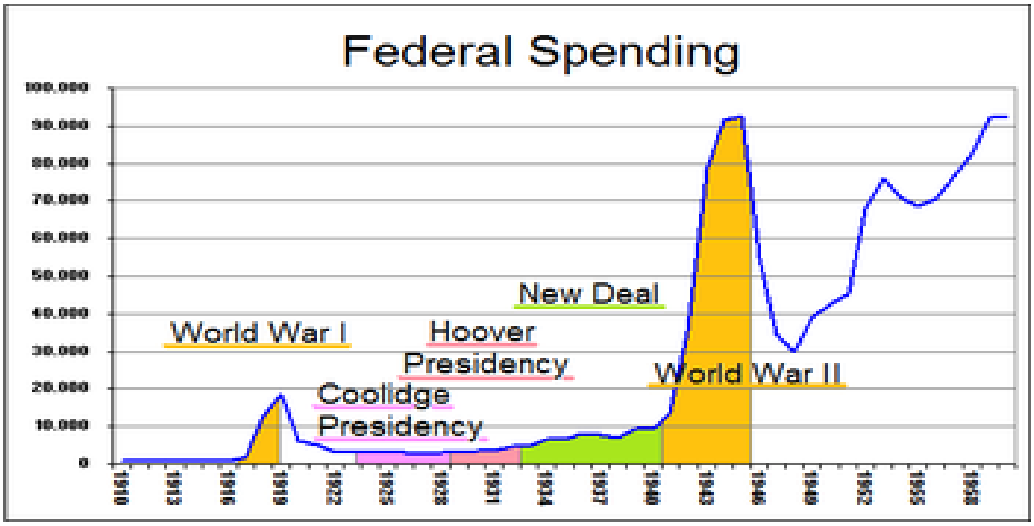
In economics, deflation is a decrease in the general price level of goods and services. Deflation occurs when the inflation rate falls below 0% (a negative inflation rate). Inflation reduces the real value of money over time; conversely, deflation increases the real value of money – the currency of a national or regional economy. This allows one to buy more goods and services than before with the same amount of money. Economists generally believe that deflation is a problem in a modern economy because it may increase the real value of debt, especially if the deflation was unexpected. Deflation may also aggravate recessions and lead to a deflationary spiral.

CAUSES OF ECONOMIC DEPRESSION

The Stock Market Crash of 1929. Many believe that the stock market crash that occurred on Black Tuesday, October 29, 1929 is one and the same with the Great Depression.

- Bank Failures
- Reduction in Purchasing Across the Board
- American Economic Policy with Europe
- Drought Conditions
- World War





BUSINESS ECONOMIC CYCLE

The business cycle or economic cycle is the downward and upward movement of gross domestic product (GDP) around its long-term growth trend. The length of a business cycle is the period of time containing a single boom and contraction in sequence. These fluctuations typically involve shifts over time between periods of relatively rapid economic growth (expansions or booms), and periods of relative stagnation or decline (contractions or recessions). Business cycles are usually measured by considering the growth rate of real gross domestic product. Despite the often-applied term cycles, these fluctuations in economic activity do not exhibit uniform or predictable periodicity.

ECONOMIC CRISIS

Sismondi and his contemporary Robert Owen, who expressed similar but less systematic thoughts in 1817 Report to the Committee of the Association for the Relief of the Manufacturing Poor, both identified the cause of economic cycles as overproduction and under consumption, caused in particular by wealth inequality. They advocated government intervention and socialism, respectively, as the solution. This work did not generate interest among classical economists, though under consumption theory developed as a heterodox branch in economics until being systematized in Keynesian economics in the 1930s.N Sismondi's theory of periodic crises was developed into a theory of alternating cycles by Charles Dunoyer,[and similar theories, showing signs of influence by Sismondi, were developed by Johann Karl Rodbertus. Periodic crises in capitalism formed the basis of the theory of Karl Marx, who further claimed that these crises were increasing in severity and, on the basis of which, he predicted a communist revolution.

UNEMPLOYMENT

The unemployment rate is a measure of the prevalence of unemployment and it is calculated as a percentage by dividing the number of unemployed individuals by all individuals currently in the labor force. During periods of recession, an economy usually experiences a relatively high unemployment rate. According to International Labour Organization report, more than 200 million people globally or 6% of the world's workforce were without a job in 2012.

CREDIT

Credit is the trust which allows one party to provide money or resources to another party where that second party does not reimburse the first party immediately (thereby generating a debt), but instead promises either to repay or return those resources (or other materials of equal value) at a later date. In other words, credit is a method of making reciprocity formal, legally enforceable, and extensible to a large group of unrelated people. The resources provided may be financial (e.g. granting a loan), or they may consist of goods or services (e.g. consumer credit). Credit encompasses any form of deferred payment. Credit is extended by a creditor, also known as a lender, to a debtor, also known as a borrower. Credit does not necessarily require money. The credit concept can be applied in barter economies as well, based on the direct exchange of goods and services. However, in modern societies, credit is usually denominated by a unit of account.

BANKRUPTCY

Bankruptcy is a legal status of a person or other entity that cannot repay the debts it owes to creditors. In most jurisdictions, bankruptcy is imposed by a court order, often initiated by the debtor. Bankruptcy is not the only legal status that an insolvent person may have, and the term bankruptcy is therefore not a synonym for insolvency. In some countries, such as the United Kingdom, bankruptcy is limited to individuals, and other forms of insolvency proceedings (such as liquidation and administration) are applied to companies. In the United States, bankruptcy is applied more broadly to formal insolvency proceedings.

TRADE

Trade, or commerce, involves the transfer of goods or services from one person or entity to another, often in exchange for money. A network that allows trade is called a market. The original form of trade, barter, saw the direct exchange of goods and services for other goods and services. Barter is trading things without the use of money. Later one side of the barter started to involve precious metals, which gained symbolic as well as practical importance. Modern traders generally negotiate through a medium of exchange, such as money. As a result, buying can be separated from selling, or earning. The invention of money (and later credit, paper money and non-physical money) greatly simplified and promoted trade. Trade between two traders is called bilateral trade, while trade between more than two traders is called multilateral trade. Trade exists due to the specialization and division of labour, in which most people concentrate on a small aspect of production, but use that output in trades for other products and needs. Trade exists between regions because different regions may have a comparative advantage (perceived or real) in the production of some trade-able commodity—including production of natural resources scarce or limited elsewhere, or because different regions' size may encourage mass production. As such, trade at market prices between locations can benefit both locations. Retail trade consists of the sale of goods or merchandise from a very fixed location, such as a department store, boutique or kiosk, online or by mail, in small or individual lots for direct consumption or use by the purchaser. Wholesale trade is defined as the sale of goods that are sold as merchandise to retailers, or industrial, commercial, institutional, or other professional business users, or to other wholesalers and related subordinated services.

DEVALUATION

In modern monetary policy, devaluation is an official lowering of the value of a country's currency within a fixed exchange rate system, by which the monetary authority formally sets a new fixed rate with respect to a foreign reference currency or currency basket. In contrast, depreciation is a decrease in a currency's value (relative to other major currency benchmarks) due to market forces under a floating exchange rate, not government or central bank policy actions. A central bank maintains a fixed value of its currency by standing ready to buy or sell foreign currency with its own currency at a stated rate; devaluation is a change in this stated rate that renders the foreign currency more expensive in terms of the home currency. The opposite of devaluation, a change in the fixed rate making the foreign currency less expensive, is called a revaluation. Related but distinct concepts include inflation, which is a market-determined decline in the value of the currency in terms of goods and services (related to its purchasing power). Altering the face value of a currency without reducing its exchange rate is a redenomination, not a devaluation or revaluation.

DEFLATION

In economics, deflation is a decrease in the general price level of goods and services. Deflation occurs when the inflation rate falls below 0% (a negative inflation rate). Inflation reduces the real value of money over time; conversely, deflation increases the real value of money – the currency of a national or regional economy. This allows one to buy more goods and services than before with the same amount of money. Economists generally believe that deflation is a problem in a modern economy because it may increase the real value of debt, especially if the deflation was unexpected. Deflation may also aggravate recessions and lead to a deflationary spiral.

FINANCIAL CRISIS

A financial crisis is any of a broad variety of situations in which some financial assets suddenly lose a large part of their nominal value. In the 19th and early 20th centuries, many financial crises were associated with banking panics, and many recessions coincided with these panics. Other situations that are often called financial crises include stock market crashes and the bursting of other financial bubbles, currency crises, and sovereign defaults. Financial crises directly result in a loss of paper wealth but do not necessarily result in significant changes in the real economy (e.g. the crisis resulting from the famous tulip mania bubble in the 17th century). Many economists have offered theories about how financial crises develop and how they could be prevented. There is no consensus, however, and financial crises continue to occur from time to time. As a result, banking institutions are typically subjected to rigorous regulation, and bank failures are of major public policy concern in countries across the world.

BANK FAILURE

A bank failure occurs when a bank is unable to meet its obligations to its depositors or other creditors because it has become insolvent or too illiquid to meet its liabilities. More specifically, a bank usually fails economically when the market value of its assets declines to a value that is less than the market value of its liabilities. The insolvent bank either borrows from other solvent banks or sells its assets at a lower price than its market value to generate liquid money to pay its depositors on demand. The inability of the solvent banks to lend liquid money to the insolvent bank creates a bank panic among the depositors as more depositors try to take out cash deposits from the bank. As such, the bank is unable to fulfil the demands of all of its depositors on time. Also, a bank may be taken over by the regulating government agency if Shareholders Equity (i.e. capital ratios) are below the regulatory minimum. The failure of a bank is generally considered to be of more importance than the failure of other types of business firms because of the interconnectedness and fragility of banking institutions. Research has shown that the market value of customers of the failed banks is adversely affected at the date of the failure announcements. It is often feared that the spill over effects of a failure of one bank can quickly spread throughout the economy and possibly result in the failure of other banks, whether or not those banks were solvent at the time as the marginal depositors try to take out cash deposits from these banks to avoid from suffering losses. Thereby, the spill over effect of bank panic or systemic risk has a multiplier effect on all banks and financial institutions leading to a greater effect of bank failure in the economy. As a result, banking institutions are typically subjected to rigorous regulation, and bank failures are of major public policy concern in countries across the world.

PANIC ON NPA

A RBI report of July 1999 made the pertinent observation, “In some countries, all or bulk of banks' provisions are general provisions and identified losses are written off at an early stage. Banks in these countries carry very little NPAs in their Balance Sheets. The recovery measures are also expeditious in view of stringent bankruptcy and foreclosure laws. It is the insolvency and bankruptcy Code (IBC) the magic bullet to shoot down the deadly Non-Performing Assets (NPAs).The IBC Board has also announced the fast tracking of cases dealing with NPAs. It has however to be understood that the insolvency law is not meant only for handling the NPA crisis. It would be short-sighted if the purpose of the insolvency law is not understood in the context of a market economy, as having broader implications. The finance ministry and Reserve Bank of India (RBI) and public sector banks (PSBs) always believe so. The finance ministry had said in its official note on May 11, 2016: “This is considered as the biggest economic reform next only to GST.IBC was meant to create a friendly and supportive environment for businesses. The point is made clear in the official note: “The vision of the new law is to encourage entrepreneurship and innovation. Some business ventures will always fail, but they will be handled rapidly. Entrepreneurs and lenders will be able to move on, instead of being bogged down with decisions taken in the past. There is a sudden note of cheer in the bleak street of financial dead-end.IBC came into force last May but it took a year for the government to issue the Banking Regulation Ordinance this May , empowering RBI to direct banks to deal with companies whose debts have gone bad through the bankruptcy law. It was found that 12 of the biggest accounts of the "top 500 exposures", accounting for 25% of NPAs, will come under the insolvency law. Of course, the bad debt will not disappear overnight. There is an elaborate process to be gone through, and it is complicated enough. The intriguing question that pops up is this: Why did it take so long for the government to have discovered the virtues of an insolvency law? It was on the anvil since 1999. The problem of NPAs requires sober analysis. It has to be understood that unlike in the US where the sub-prime mortgage crisis of 2007-08 - NPA under a different name - brought the big banks down and forced the US Federal Reserve to put in place a humongous bail-out package, in the Indian context the banks have not broken under the burden of NPAs. So the chest-beating over NPAs needs to be subdued, and there is need for informed criticism. There are two important issues that are likely to be glossed over in the concern over NPAs. First, all NPAs are considered mala fide. That is, it is assumed that banks and borrowers had conspired to defraud public money and they were not sincere in making the business ventures for which the loans were taken a success. The motive cannot be ruled out, especially with regard to government-backed infrastructure projects. But there is need to acknowledge the risk factor in a market economy: unless you dare to fail you will not succeed. Of course, risk cannot be treated cavalierly but needs to be subjected to rules of commercial prudence. RBI figures show that in 2014-15 NPAs constituted 4.3% of gross advances and 2.7% of total assets in of the scheduled commercial banks. In case of PSBs the corresponding figures were 5% and 3.2%. As a matter of fact, the situation in 2014-15 was much better than it was in 2003-04. The figures for 2003-04 were 7.2% of gross advances and 3.3% of total assets for the SCBs, and 7.8% and 3.5% for the PSBs. In absolute terms the moneys involved would run into thousands of crores, but in the context of the transactions of the banking system, the figures assume a more realistic proportion. The central bank's figures for NPAs from 1993 to 1998 show that the situation in those years was far more critical. The figures speak for themselves. Total NPAs: 23.2% (1993); 24.8% (1994); 19.4% (1995); 18% (1996); 17.8% (1997) and 16% (1998).One of the arguments made in the last five years has been that credit off take from the banks in general and PSBs in particular was inhibited by the monstrous presence of NPAs in the balance sheets.

CONCLUSION

The New Deal did not end the Great Depression. Indeed, the Roosevelt regime ran consistent budget deficits of around 5% of GDP from 1931 onwards, spending twice as much as tax revenue. And the government took on lots more workers on programmes – but all to little effect. Coming off the gold standard and devaluing currencies did not stop the Great Depression. Indeed, resorting to competitive devaluations and protectionist tariffs and restrictions on international trade probably made things worse. And monetary easing has not worked this time and nor has fiscal stimulus (as Abenomics in Japan has shown), which we shall see again if Trump ever does manage to run budgets deficits to lower corporate taxes and increase infrastructure spending. Now it seems protectionism and devaluations are becoming more likely in this post-Trump, post-Brexit period of the Long Depression. Indeed, the latest policy document for the G20 summit held in Germany last week has actually dropped its condemnation of protectionist policies. While there is no doubt that the issue of NPAs needs to be managed quickly and efficiently, there is need to change the basic attitude towards losses and failures. The Indian economy cannot blossom if it cannot take failures and losses in its stride. India, its people, government and business folk have to give up aversion to risk if the country is to move ahead. They have concentrated on the growth potential of his plans for tax cuts and higher infrastructure spending, rather than his threat to build a wall along the Rio Grande and to slap tariffs on Mexican and Chinese imports. Then government took over from the private sector in directing investment and employment and using the savings and consumption of the people for the war effort. Profitability of capital rocketed and continued after the end of the war. Looking back, the depression of the 1880s and 1890s in the major economies only ended after a series of slumps finally managed to raise the profitability of capital in the most efficient sectors and national economies and so delivered more sustained investment – although eventually that led to imperialist rivalry over the exploitation of the globe and the first world war.

REFERENCES

[1] Acharya S. (2009) Gloabal crisis, India and Agriculture, 9th convocation, Rajasthan Agriculture University (RAU).

[2] Chandrasekhar C.P. and Ghosh Jayanthi (2008) India and the Global Financial Crisis. From http://www.macroscan.org.

[3] Chidambaram P. (2008) Spill - over effects of global crisis will be tackled. The Hindu, Daily, 15.

[4] Conway E. (2009) WEF, Global crisis has destroyed 40pc of world wealth, Internet edition.

[5] Field, Alexander J. (2011). A Great Leap Forward: 1930s Depression and U.S. Economic Growth. New Haven, London: Yale University Press. ISBN 978-0-300-15109-1..

[6] Economic survey of India, 2011.

[7] Field, Alexander J. (2011). A Great Leap Forward: 1930s Depression and U.S. Economic Growth. New Haven, London: Yale University Press. p. 182

[8] Green D., King R. and Dawkins M.M. (2010) Impact and Response, Oxfam Research Report.

[9] Horn Z.E. (2010) Women in Informal Employment, Globalizing and Organizing (WIEGO).

[10] IMF (2011) World economic outlook update, rapidly weakening prospects call for new policy stimulus. Washington, DC.

[11] RBI's Bulletin (2011) Foreign Investment Inflows, Table No. 44.

[12] Seshan P.A. (2008) Concern over impact of U.S. crisis, The Hindu, 44.