Effectiveness of the counter cyclical policy

Introduction

The focus of this study is on the extent to which the monetary and fiscal policy was used during the great recession. The great recession started in 2007 and ended in 2009. It was triggered by the financial crises that occurred in the mortgage and banking sector in the United States of America. The study also focuses on how the monetary and fiscal policy has been employed to date with an aim of moderating the business cycle. In particular the study focuses on the housing markets. Data sets on housing market has been presented in the excel sheets and thoroughly analyzed.

Economic and sociological forces

**Reasons that drove the market equilibrium to unsustainable heights (bubbles)**

A bubble refers to an economic cycle that is characterized with rapid shift in the asset prices which is then followed by a contraction. It is influenced by the social and economic factors affecting an asset and the market behavior. When there is an economic bubble the market prices and activity shifts significantly rendering the forces of demand and supply incapable of setting the market prices. The changes in the asset prices and activities are presented in the trends presented in the excel sheet

There are multiple factors that brought the housing market to unsustainable heights. A key cause of the bubble was the housing speculation. This led to subprime lending in the mortgage sector to individuals who could hardly afford the houses resulting in excessive supply of houses and low demand after the crises. Poor credit agencies ratings led to individuals without debt repayment capability gaining access to these houses. Excessive supply of housing thus ended up pushing the prices of housing down.

**Shocks that brought the market back down**

There are various factors that led to the cooling effect of the housing market in the US. For instance, the government economic stimulus led to an upturn of the US economy something that boosted the economy up. This resulted in increased household income and ability of people to repay mortgages and afford housing increasing demand in the housing market thus pushing prices up. Stringent policies by Federal Reserve Bank on lending, that emphasized on more due diligence also played an important role in cooling down the housing bubble.

Changes in the demand and supply in the housing market in US 2007-2019. This is evident from the data sets presented in the excel sheets for the four indicators between 2007 and 2019 as indicated in this section

Between 2007 and 2019, the demand and supply of houses in the US changed significantly. This is evident from the data presented in the

Changes in demand and supply in the housing market

**Housing starts**

The data on the housing starts indicates the total number of privately owned houses that were started between 2007 and 2019. As indicated in the data, the number of newly established privately owned homes was very high between 2007 and the end of the 2008. When the supply goes up, the price of the products goes down. As many financial institutions invested in the mortgage market, many of the residents gained access to housing, although many of them could not later afford to service the mortgages. The number of private houses thus significantly declined between 2009 and 2014 before it assumed an upward trend towards 2019 as the housing bubble was subdued. The increased number of private owned houses between 2014 and 2019 was as a result of the US economic recovery.

House hold income

Between 2007 and 2009, house hold income declined. The trend continued until 2013 when it assumed an upward trend. It has continued to increase towards 2019. When there is increase in the level of income in the economy, the demand for houses increases. As a result, the supply also goes up.

Unemployment rate

The unemployment rate sharply went up between 2007 and 2011 before it assumed a downward trend to date. The decline in unemployment rate was as a result of the recovery of the US economy from the 2007 great recession. Increased employment has increased purchasing power and demand of housing in the US towards 2019 increasing housing supply and the price levels.

Housing prices

The housing prices were low between 2007 and 2009, slightly declining from the 2006 levels. As a result, many financial institutions invested in the housing market resulting in excessive supply of houses and sale to people who could hardly to afford them. The enhance US economy has pushed housing demand, supply and the prices up.

Specialization of industry and impact on recession

The housing market has unique factors that contributed towards the recession. The real estate industry is known to pay off due to their long horizon of investment. As a result, funds are drawn from other sectors and directed to the industry. This was the case in the 2007 when high level of liquidity was directed to the industry denying other industries financial resources necessary for production purposes.

Prior government policies and legislations that might have exacerbated the shocks

The federal agencies have always promoted access to housing among the residents. The 1977 Community Reinvestment Act extended this idea. This led to the development of less stringent standards that adversely affected the housing market. Ineffective federal regulations on the minimum level of liquidity that commercial banks should retain equally adversely affected their operations. Excessive mortgage lending resulting in low liquidity levels in commercial banks something that pushed their level of liquidity significantly down. Higher consumer debts led to unsustainable financial system. Proper control of the liquidity levels in the banking sector could have been necessary in preventing the housing bubble that occurred in 2007 in the US.

Government actions and regulations that were initiated to address the situation

The government stimulus policy was adopted as the 2007 great recession was realized. The stimulus was aimed to boosting economic growth and increased employment levels among other macroeconomic goals.

Government fiscal policies and federal monetary policies necessary to address the situation- responses

Effectiveness of the countercyclical policies adopted

Conclusion