

Psychological Effects of Economic and Financial Crises on the Behaviour and Mental Health of Individuals

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Abstract

The present paper brings forward the psychological effects of the financial and economic crisis upon individuals. Following the empirical research as well as the specific literature, we discovered that the greatest psychological effect of the financial crisis upon individuals is created by the financial stress. Moreover, the study shows that the financial stress, as a psychological effect of the financial crisis, is associated with the fear of not being able to accomplish the financial needs, the impossibility to have a high standard of living, a lower self-respect and the withdrawal form former social groups.

Key words: psychological effects, financial and economic crisis, behaviour, financial stress, mental health.

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1. Globalisation and financial crises

The moment when globalisation exacerbated, financial crises appeared. These crises reveal the price instability on the financial markets, as well as the "lack of cash", without which the geo-economic system cannot function. Throughout history, examples of economic crises are numerous and unpleasant, but the world economy "memory" has only kept the following: the great stock market crash (The Wall Street Crash) in 1929 which triggered "the great recession" that lasted until 1933; the stock market crash in 1987, which was the greatest crash recorded in a single day, and then there are the emergent markets crises of the 90's

which involved significant geopolitical and economic repercussions.

At the moment we are in the middle of the most serious financial crisis compared to the great 1929-1933 crisis. At a glance, this crisis, which started in the USA, resembles the others very much, but there is also one significant element which makes the difference: it designates the end of an era of credit expansion, which has the dollar as a currency reference [1]. The US government wish for the Americans to be able to buy a house has forced FED to cut the refinancing interest rate of commercial banks by 1% a year since the 90's. Given these facts, banks granted credits with an interest rate of 2-4% a year, which led to an unprecedented "real-estate boom". Since 2000 and until 2005 we assisted at a real-estate frenzy that was supported by a market quota increase of over 50%. This overwhelming increase actually favoured speculations on the value of both the houses and the loans. Thus, when we expect the house value to be higher than the loan, the tendency is to purchase as many estates as possible (in 2005 more than 40% of the real estates were holiday residences or investments). Since 2005, the inflation danger which was threatening the USA, forced FED to increase the interest rate up to 5% a year. Therefore, commercial banks operated an interest rate rise of 6-8% a year. These doubled or even tripled interest rates have led to the impossibility of instalment payments and to foreclosures [2]. Thus, millions of people couldn't cope with FED's new interest rates, and banks suddenly found themselves in the possession of an impressive number of houses, which they tried to auction, thus unbalancing the interbanking relations. The major cause that created the crash in the international banking relations

was the fact that American banks succeeded their refinancing by selling the high risk real estate contracts (the contracts with a low payment capacity of the population) to other worldwide investment banks (UBS-Switzerland, Deutsche Bank - Germany). *What did the other countries hope for regarding the crisis?* The answer is simple. They wished to avoid contagion, which developed during the crises in the 90's. But the story seems to have repeated, and the whole world economy “is catching the American flu”. Contagion, or the domino effect seems to function really well [3]. In the US, the economic crisis started in 2007, while the European and the continental economies were perfectly going on. Now, after five years, the international media announces significant downsizing in many states and on different continents.

2. Psychology and human behaviour

Psychology is a developing science with the goal to understand, discover and explain human nature – the mental process and the behaviour which make us what we are and separates us from other beings. Personality psychology, which is part of social psychology, studies the influences of information, situations and of other individuals on people and tries to understand the changes of personality caused by them. That is, personality psychology investigates the individuals' ideas, feelings and behaviour.

Behaviour is the externally observable response of a person to an environmental stimulus. According to psychology, behaviour presents an intellectual feature, as well as an intentional and an emotional one [4].

Behaviour, which depends both on the individual and on the environment, but mostly on the economic environment, always makes sense. It corresponds to seeking a solution or an object likely to reduce the needs of the individual. In the economic literature, classical and neoclassical theories describe man as rational and able to make the best decision. This “perfect man” was called *Homo economicus* [5]. Meanwhile, research determined *homo economicus* “to change his style”, which led to the dissolution of a rational *Homo Economicus*. The change of

style was supported by the development of the *limited rationality* that considers human beings as unable to make efficient decisions because they cannot have all the data and do not efficiently anticipate the outcome. Thus, if we take limited rationality into account, we may say that the greatest psychological effect of the crisis upon the individuals is the financial stress.

3. Financial stress

According to the *American Psychological Association*, the most common source of stress is money, or the lack of money [6]. Is present in people's life from all social classes and it appears where the individual cannot cope with changes.

Generally, stress may be defined as an unpleasant feeling that appears with the fear of loss or when threatened by something such as economic and financial crises, which are external stress factors to individuals. More precisely, financial stress may be perceived as breach in the daily program of both the individuals and the financial markets [7].

According to Chinese culture, risk has a double meaning, being a combination between danger (crisis) and opportunity. Following this line, we may interpret financial stress in the same dimension.

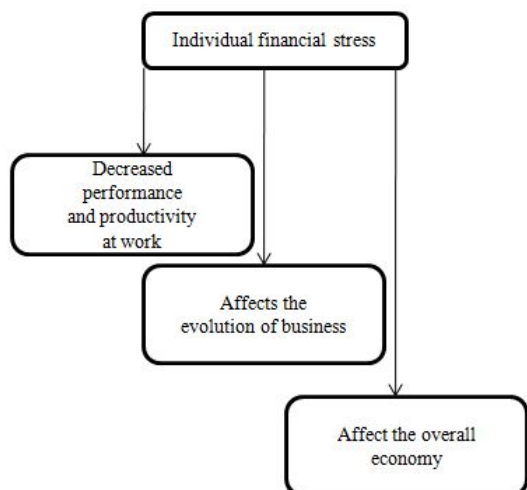
- *Financial stress as danger*. Financial stress is different from one person to another and it may appear under several forms, starting with the threat to lose one's job. Such features are: the fear of being unable to meet one's financial needs, a lower standard of living, a lower self-respect and the withdrawal from former social groups when financial stress appears.
- *Financial stress as opportunity*. Financial stress may also lead to positive changes in one's life: finding a job, or improving the ability to manage personal finances.

The intensity of the financial stress is mostly measured by the lapse of time which postpones the purchase of household appliances, the rhythmic payment of bills (a major stress factor), the decrease of the living standard, the lack of cash flow, the possibility to lose one's job [8].

Generally, it is very difficult to assess the cost of financial stress for both the individual and the society as a whole. However, the cost

may be set according to the effects that financial stress has upon the individual mental health, as well as upon the economy. Within the economy, financial stress may reduce job performance and productivity, thus creating a gap within the business development and the general economic system.

Figure 1. The individual financial stress outcome



Source: Authors' research

4. The impact of the economic crisis upon the individuals' mental health

Sanity is very important as it allows the individuals' personal development in the emotional, psychological, intellectual and social dimensions. Moreover, it is beneficial for the job atmosphere, in order to determine an economic growth and a social development.

It is expected that an economic crisis affect the mental health of the individuals. Sanity problems caused by the economic crises produce chaos in the community, within the country, and at the level of world economy.

Table 1. The significant element of the population's sanity

Protection factors	Risk factors
Social capital and social protection	Poorness and high debts
Children's health before and after birth	Unhealthy food, mental health heredity

Balance at work and at home	Unemployment, job insecurity, stress at work
Healthy life style	Alcohol and drug addiction

Source: World Health Organization, *Impact of economic crisis on mental health, 2011*

The different personality features of individuals make them react differently when facing the economic crisis. Thus, they may experiment a constant search to find solutions to overpass the crisis, they may ask for extra state incentives or social protection, or they may increase consumption and ignore the crisis. On the other hand, they may develop anxiety issues and display nervous breakdowns due to a constant feeling of helplessness.

The world economic situation demonstrates that the crisis started in 2007 affected the population on three different channels:

- *Channel 1 – the stock exchange and the real-estate market* (this level has affected the investors who had resources and invested in securities or over-the-counter derivatives, but also on the estate market);
- *Channel 2 – banks* (this category includes people who have financed their purchases by obtaining bank loans);
- *Channel 3 – pay cuts and layoffs* (it affected people whose salaries decreased and those who lost their jobs due to downsizing or to bankruptcy) [9].

According to World Health Organization studies, the present crisis has significantly affected Europe. Thus, Europeans lost their jobs and the vulnerable groups, such as people with low incomes and very poor people, were socially excluded. World Health Organization includes children, single parent families, unemployed people, ethnic minorities and old people among the vulnerable groups. Poorness affects children in their cognitive, emotional and physical development, as well as their life-long health and wealth [10].

Besides the negative effects of the economic crisis on the individuals' mental health, there is also the opportunity to strengthen economic policies of social support.

The health system cannot assure the individuals' sanity without the help of the

state. Thus, the side effects of the economic crisis may be diminished by economic policy measures:

- creating active programs for the labour market (programs to keep jobs, or requalification programs to reintegrate people on the labour market, special programs for young, unemployed or disabled people);
- family support programs (support for further study, for maternity leave and for the child-raising leave);
- a significant increase of the alcohol price, as well as lower distribution, which determines a decrease of alcohol consumption;
- medical assistance for people with a high risk of mental health problems;
- programs to cut people’s debts to the state.

5. The psychological impact of the economic crisis upon the Romanians

Nowadays, Romania – an emergent economy with severe systemic problems (inflation, unemployment, corruption, education, EU funds absorption, infrastructure, and loan-dependent) which is open to the external market – was deeply affected by the present unfavourable economic situation.

Connecting the Romanian economy to the international economic flows favoured the development of contagion (generated by the US sub-prime crisis) inside Romania. The moment the sub-prime crisis burst continues the *timeline design* of the other economic and financial crises.

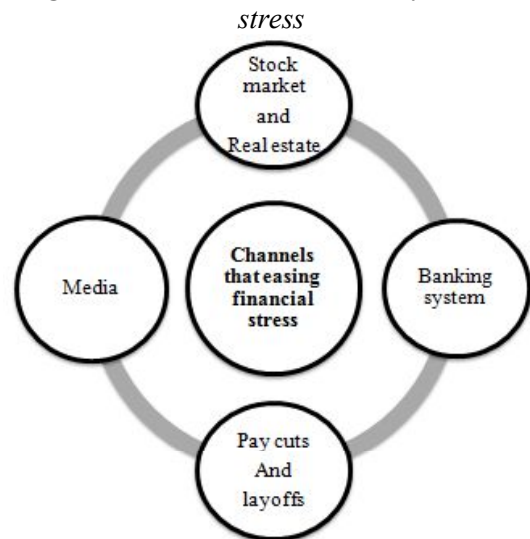
According to the *Oxford Dictionary*, the term “contagion” is defined as the communication of disease from one person to another by close contact. However, the word comes from Latin and is made up of *con* (with) and *tangere* (touch) [11]. *The theory of contagion* which was developed by Mori Kogid și Kok Sook Ching in 2009, demonstrates that no country in the affected region cannot avoid contagion of such an economic crisis... [12].

After 8 years of economic (2000 - 2008) and very sure on itself, Romania is now dealing with the reverse situation which has a major psychological impact upon Romanian consumers and investors. Thus, due to a long

lapse of economic growth, the present economic crisis is psychologically difficult and rather impossible to accept for the Romanians.

The channel that favoured the appearance of the financial stress in the case of Romanian consumers and investors are the same (the stock exchange, the real-estate market, the pay cuts and layoffs). However, we wish to add a fourth level that has a major psychological impact on the Romanian population, and that is *the media*.

Figure 2. The channels that send financial stress



Source: Authors' research

The year 2008 came with the same crisis situation for the Romanian Stock Exchange and determined the decline of the equity market. The equity market faced two important phenomena that had a negative impact on the investors:

- institution investors were out of the market until the emergence of positive signals on the market evolution;
- risk aversion, Romanian investors preferring to protect themselves against any risk which could threaten their investment.

The investments on the real-estate market that were based on *buy cheap, sell expensive* have worked until mid-2009, when investors considered them *a free lunch*. Starting with June 2009 and until June 2010, real estate investments started to record a major decrease, with a 30-40% loss of the investment.

Banks represented the second channel that

had a psychological impact on the population. Actually, this channel is closely connected to the third one, which deals with pay cuts and layoffs. Most Romanians have asked for bank loans in order to purchase real estates or household equipment. Pay cuts and layoffs do nothing but higher the risk of default of borrowers to banks, thus causing losses on both sides: borrowers are left without estates or purchased goods, and banks face foreclosure.

Just as the economic crisis, the media is a constant figure in people's lives and it has a significant psychological effect on the population, because the human brain processes the information according to word utterance, attitude and voice volume. In the article “What are the psychological effects of the financial crisis?” published in Psychologies Magazine, Radu Crăciun, investment manager at Eureko Pensions, considers that: “there is a terrible “noise” in the media regarding the crisis. It is a situation where professional opinions, rational and non-biased voices cannot be heard at all. Unfortunately, people look for the extreme and farcical opinions, as the decent ones are not “spicy” enough for the audience. This media bombardment artificially augments the stress factor and creates misinformation”.

6. Conclusions

The effects of the economic crisis are numerous and omnipresent, thus creating vulnerability within the daily activities. Therefore, we can say the appearance of an economic crisis triggers important changes for the individuals on the one hand, and represents a major challenge for the governments dealing with the crisis. Hence, it is very important to model efficient measures in order to overcome the economic crisis (creating active programs for the labour market, medical assistance for people with a high risk of mental health problems, programs to cut people's debts to the state, reintegrating the unemployed on the labour market). Moreover, there are other important measures that help people to overpass the economic crisis, such as promoting stress management by psychological support as well as professional career guidance systems.

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