

EC1B5 Winter Term 2023-24

Answer Key to Discussion Question 8 (Week 10 Class)

Week 10 class: How does the housing market contribute to the great recession through its effect on consumption demand and banks failure?

Answer key:

Consumption demand: Demand for consumption had decreased due to the following reasons:

- a. job loss in construction sector,
- b. drop in housing wealth, and
- c. ability to borrow due to drop in collateral value of houses.

Bank failure: The pre-recession housing boom had encouraged uptake of sub-prime mortgage which contribute to the huge amount of default during the recession after the house price collapsed. Many of these sub-prime mortgages were packaged together with other assets through “securitization”, this is why many banks are affected.