UNIT Monash: Week Three Newsletter

Hey <<First Name>>!

For our loyal readers, we bring to you the third instalment of our throwback market wrap series.

Have you ever wondered what the so-called housing bubble was and how it caused the Global Finance Crisis?

Sink your teeth into this week's newsletter and find out!

Throwback Market Wrap

A Brief Summary of the GFC

What do a house and a ninja have in common?
It may not be what you think, but both things contributed to one of the most significant and horrifying events in modern history and brought us close to a global apocalypse. The funny part is, it happened not with aliens, or with nukes, or with guns. It happened, on a clear sunny day in 2008. And no one, except for a few, saw it coming.

As common knowledge would tell you, loans can only be made if the person borrowing the money can pay it back. In America, that was the case for a long time until mortgage brokers (the people who match those who want to buy a house to those who wanted to lend them the money to do so) and lenderslaxed their due diligence and approved loans to anyone, even if they couldn't afford it. Paired with their legal right concerning bankruptcy; that a person merely needs to drop their house keys at the front entrance to declare bankruptcy and no longer be liable for legal proceedings.

Enter the ninjas.

NINJA (No Income, No Job, No Assets) loans entered the market like wildfire. Brokers made suitcases of money just by introducing the two parties and lenders made their profits by handballing their risk of bad loans to unsuspecting investors in the form of a CDO (Collateralised Debt Organisation)[1]and making their loan principal back (with a fee of course). The best part about the CDO was that banks could cherry-pick their loans that they would like to keep and pack the CDO with unwanted loans while the credit rating agencies rated these instruments as investment grade.

It was an unlimited cash machine for a while. And then, tragedy struck. The ninjas couldn't honour their loans, and the unlimited cash machine turned into the financial horsemen of the apocalypse. The lenders (both banks and smaller private lenders) defaulted on a substantial part of their loans and could not break even on loans present in their balance sheet. Furthermore, those who invested in the CDOs included both investment firms as well as banks and resulted in huge losses as it turned out that all the loans in the CDO had abysmal individual credit ratings, even though the instrument itself received an investment-grade rating.

The result of the crisis was catastrophic: several banks were urged to merge by the government to prevent the whole bank system from collapsing and reducing the effects of contagion[2]. Furthermore, the GFC lead the long-standing financial firm, Lehmann Brothers, to close its doors after failing to reach a mutual agreement to merge with the other banks. Thousands of workers lost their jobs directly as a result of the crisis, with millions of others affected by the severe economic downturn. This also reached other parts of the world too, with Australia, Europe and Asia having difficulties in the financial sector (of which many argue that the GFC influenced the subsequent Eurozone crisis).

Alongside the economic effects, the GFC revealed to the world the extent to which greed and recklessness dominated the banking profession. News surfaced of one of the world's largest Ponzi schemes carried out by Bernie Madoff, in which he swindled upwards of $64 billion from his clients' accounts. Furthermore, the bailout of the banks by the American government lead its beneficiaries (mainly CEOs and top executives) to pay out generous bonuses, of which they used to go on holiday. And after all of it, only one banker in the US was found guilty.

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[1]A Collateralised Debt Organisation is an investment vehicle in which a loan or several loans can be placed. Considered as securitisation, where the loans can be offloaded for investment.
[2]Contagion is the concept where one bank defaulting would lead to other banks defaulting too. Due to the tendency for banks to lend to each other.

Weekly Global Breakdown

Australia

The Australian share market has capped off their worst week since November, despite a slightly higher finish on Friday. The sluggish week was on the back of the reignited trade feud with the fallout dampening investor confidence. Damage is currently being wreaked by the increasing trade tensions, with the trade uncertainties leaving investor's nervous and cautious about the outlook of the global economy.

In light of the modest gains on Friday, the tech sector was the only sector to post gains in excess of 1.00 per cent, closing 1.30 per cent higher. Afterpay led the way with a 6.10 per cent increase, after it announced that it had grown its customer base from 1.5 million to 2 million customers, within the space of 2 months. The mining sector produced mixed results, despite an uptick in the price of iron ore, with BHP Billiton and Rio Tinto both falling, whilst South32 finished 1.80 per cent higher.

The ASX is poised to open lower with the SPI futures pointing to a 22-point loss at open, after the trade war between the US and China continues to escalate. Many economists fear that the ongoing trade dispute may lead to a recession.

US

Wall Street stocks tumbled on Friday, after trade tensions intensified, with all three major indexes falling. The Dow Jones Industrial Average, S&P 500 and Nasdaq Composite dipped 0.34 per cent, 0.66 per cent and 1.00 per cent respectively.
The US will continue to restrict doing business with Chinese telecoms giant Huawei.
In other news, Uber Technologies reported a $US5.2 billion quarterly loss and failed to meet Wall Street expectations, with its shares sliding 6.80 per cent.

Looking ahead, a deal is a long way off from being reached between the US and China, which is igniting fears over an impending recession.

Asia

The Chinese market closed the week lower, following mounting trade tensions and softer factory data. The blue chip CSI300 index and Shanghai Composite Index dropped 1.00 per cent and 0.70 per cent respectively. Similarly, Hong Kong's Hang Seng index slid 0.70 per cent, with the ongoing protests weighing heavily on the index.

The likelihood of a trade deal being reached is becoming less and less likely. The prolonged trade war and the protests in Hong Kong are triggering growing fears of a looming recession.

Europe

The European market has extended their run of losses, with the ongoing trade dispute between the US and China and political uncertainty in Italy weighing on the market. Trump's comment that the US would not make a deal with China weakened sentiment. Further, Italy's budget crisis and fresh election worries have resulted in Italian stocks dropping 2.50 per cent.

European markets are expected to open lower on Monday, with concerns over the escalating trade tensions could lead to slower global growth. Investors will be looking to get ahold of safe-haven assets.

New to markets? Got Questions?

As we mentioned in previous emails - we started UNIT Monash with the vision of educating the student community in investing and trading to one day strive for financial independence.

We want to create a new concept of peer-to-peer communications about investing and trading. There's a lot of value in sharing experiences, having opinions and shedding light on new ideas. Feel free to get in contact with us via Facebook if you have any enquiries about investment, trading or our upcoming events or if you would like to provide any feedback.

Regards,
UNIT Monash

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