The Official D&I Newsletter

Issue: 6 February 2022

# Words of Visionaries

## Module: Financial Dooms that Shook the World

At Dreamers & Innovators, the ongoing module: "**Financial Dooms that Shook the World"** is an ambitious endeavor to help young Dreamers comprehend the technicality prerequisite to understanding national and international economies. The module aspires to build awareness of economical concepts along with coursing through three historically significant financial crises. The overall aim is to build the knowledge & skill which shall help the Dreamers to analyze the current circumstances of the Pandemic and predict where we are headed economically.

This week's newsletter showcases the ideas of four promising Dreamers: Aditya, Prisha, Pranavi, and Pranay, who provide you with a detailed study of the Great Recession which took place in 2007-09 in the USA and affected several industrialized economies globally.

Dreamers & Innovators is a knowledge and skill-building platform for 21st century learners. We aspire, design and execute interactive learning experiences where global knowledge relevant to today and tomorrow is brought to young Dreamers. At D&I, 21st century skills are honed, confident communication is developed and independent, informed opinions are nourished.

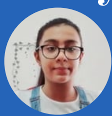
## The Great Recession of 2007-09

Aditya Bhura
14 years

The Great Recession was the next biggest financial crisis after the Great Depression in the United States of America. Also known as the Lehman Brothers' Crisis, this major crisis took place in the years 2007-2009. The crash of the investor chain led to a subsequent international banking crisis. Investment banks and major investors who had invested their money in financial instruments called CDOs did not receive their invested money back from the sub-prime lenders at that time.

The insurance companies who had promised them insurance over investment did not repay or secure these large amounts of money back to the major investors. This further fueled the whole housing market to collapse with no money to repay the loans. Several investors and investment banks went close to bankruptcy and were in grave losses, like the Lehman Brothers, AIG, and The Bank of America. This caused many banks to shut down as the demand for houses was very low but the availability was high (Also known as deflation). The consequences were that the GDP declined by 4.3%, unemployment rose to 9%, 15% of the population went below the poverty line, and the stock markets, which already had faced major damage in 'The Great Depression', fell by 57%. The Global consequences were great as the Dollar Currency is among the official currencies for forex and international trade, as recognized by the IMF. The European Debt Crisis started after this and most industrialized economies experienced an economic slowdown. This crisis was one of the worst economical declines in the US and the citizens had to face the consequences for long.

## Subprime Borrowers: a Study



Prisha Sheokand
14 years

The Great Recession was an economic downturn from 2007 to 2009 that wrecked global financial markets, banks, and real estate industries. The crisis led to an increase in number of home mortgages even to subprime borrowers which eventually led to unemployment, falling home values, and a decline in the stock market.

In 2007, US real estate markets were flooded with homes being purchased by people with low credit rating also, called the Subprime borrowers. The lenders gave out loans liberally against low cost mortgages during this real estate boom. In their desperation to sell more mortgages, the lending banks relaxed credit requirements. When people who already had trouble handling debt in the past used these loans, they landed up facing further difficulty in repayment whereas those who had good credit scores, called the Prime borrowers, could afford loans and its timely repayment. The subprime numbers soon out nubered the prime borrowers.

As values of houses(assets) slipped, many of these mortgages amounted to more than the home's total value. Many homeowners found themselves unable to afford their monthly mortgage payments. Also, they could no longer refinance or sell due to dropping real estate values leading to millions of Americans falling behind on their loan repayments with no way of escaping an inevitable default.

## USA's Menace: Credit Crisis

Pranavi Sethi
13 years

Everyone knows about money but how many of us know how to get money? One way is to earn money by working but sometimes we need a large amount of money and wish to pay later, maybe in parts. For example, if we want to buy a house then most of the time we need funds from external sources. These external sources are mostly banks and if Itake funds from a bank then I am their borrower.

The people who take loans from the bank are known as borrowers. Prime borrowers have secured jobs and incomes that suffice to pay back the loan. They have a good credit history. Whereas, subprime borrowers are those who are more likely to default on the loan do not have a suitable financial background nor do they have a sustainable job. They have a bad credit history. The prime borrowers take the loan less than the actual cost of the house. On the other hand, the subprime borrowers take the loan close to that of the actual cost of the house.
To summarize, we can say that the banks are likely to give loans to prime borrowers at a lower interest rate. Whereas banks are reluctant to give loans to subprime borrowers and even if some banks give them loans, they give them at a higher interest rate. Here is one interesting fact for you: lending to subprime borrowers and non-payment of the loans by such borrowers in America led to the Great Recession in 2008.

## Consequences of USA's Recession

Pranay Jalan
12 years

In 2007, it was realized that subprime borrowers who had bought houses through mortgaging were not able to pay back their loans, so the banks had to seize their mortgaged homes, leaving people homeless. Since so many people lost their homes, there was a supply and demand problem in housing therefore there was deflation.

Since the value of the houses was so low the banks were not able to sell the homes to make up for lost money. Investors who had invested in these homes lost a lot of money, so did the banks that had first given the loan. But the most significant loss was for investment banks such as JP Morgan, Morgan Stanley, Goldman Sachs. It was the Lehman Brother's investment bank that filed for bankruptcy and initiated the domino effect of further collapse. In addition, the credit raters and insurance companies that were bribed to lie also started going bankrupt.

Surprisingly, the US Government then used $700 billion worth of tax-payer money and gave it to some institutions to help with their bankruptcy. Some of the main services that received money from the government were: Lehman brothers, $130 billion; AIG, $180 billion; Citigroup, $25 billion; JP Morgan Chase, $25 billion; Wells Fargo, $25 billion; Bank of America, $15 billion.