2008 Financial Crisis: A Study of Trust and Strategy

Chris Ciccone

Hypotheses

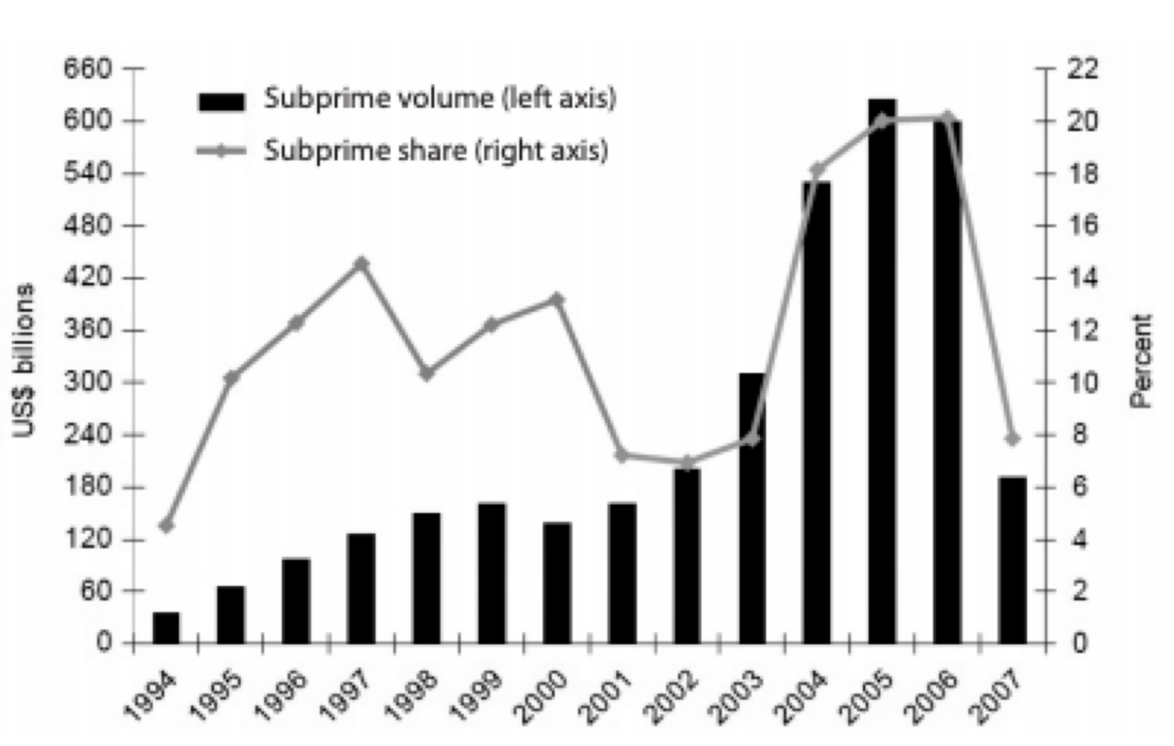
- Financial firms lost trust after 2008, had to earn it back
- Institutional investors have become more transparent and ethical
- Institutional investors have adopted safer strategies

Importance of the Market

- Social Security is not expected to be significantly helpful in retirement
- 401k plans have replaced defined benefit plans (pensions) in the private sector
- IRAs and 401k/403b plans are the most common
  - Exception for government workers
- Majority of people must rely on market to fund long term goals

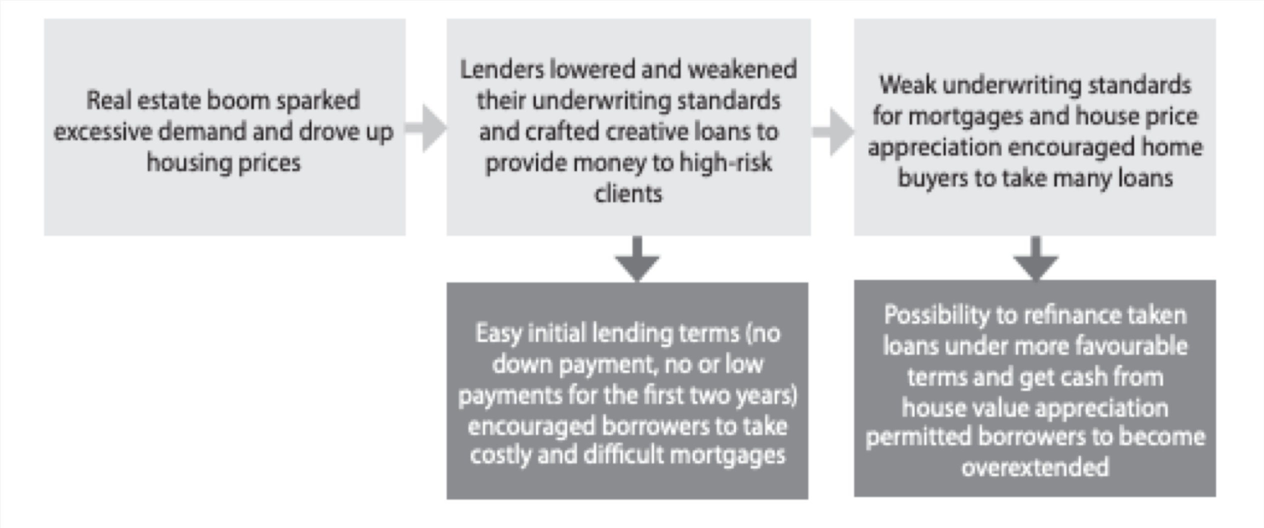
2008-2009 Financial Crisis

- Two main causes
  - Mortgage Backed Securities (MBS/CDO) and Subprime lending
    - 20% of home loans were subprime



2008-2009 Financial Crisis Pt. 2

- Housing Bubble
  - Started by low interest rates
  - Housing prices fell
  - Rates rose, subprime loans began to default



Powder Keg Explodes

- Combination of billions of securitized loans and housing bubble bursting
- MBS and CDOs fell off a cliff
  - Subprime -70%
  - Prime -20%
- Liquidity dried up
  - Forced a full blown recession
- American families did not save
  - ~50% between 2001-2004
  - Housing prices fell, forced to save in order to pay bills
- Global GDP dropped to -0.9%
  - US dropped to -2.6%

Trust and the Market

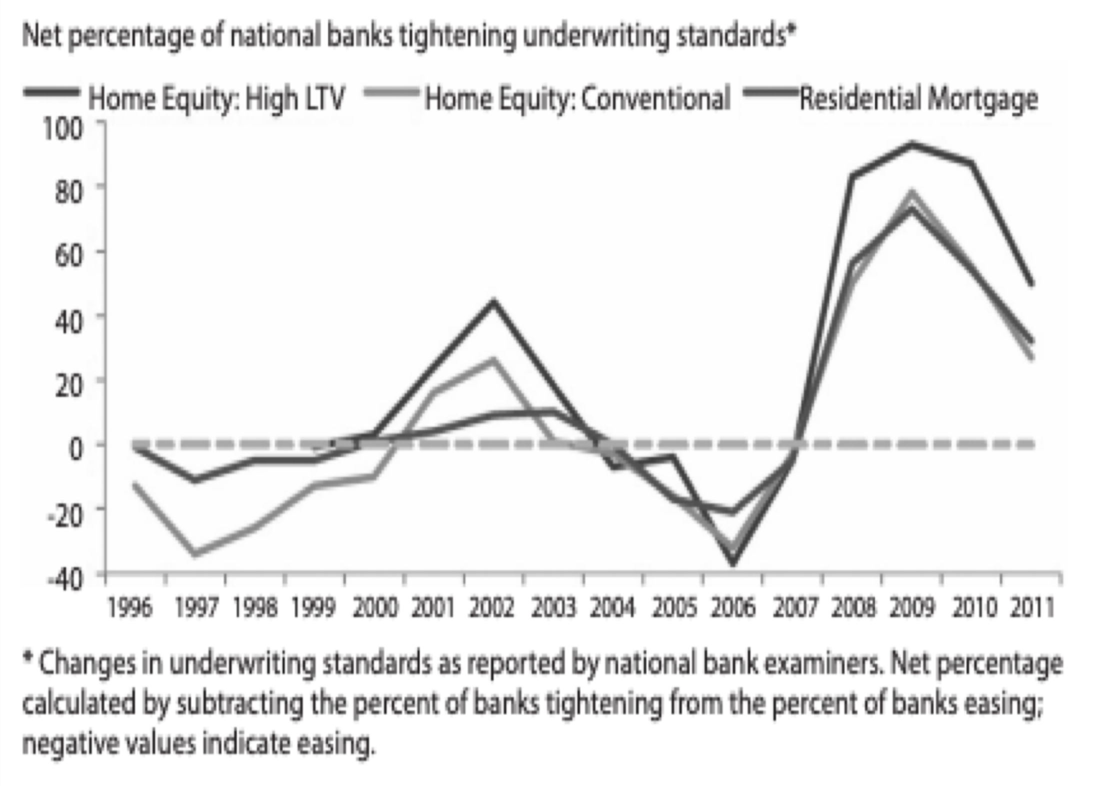
- Scandals
  - Madoff, Enron, others
    - Cost Americans over $180 billion
- 1976 40% of Americans trusted the financial system
  - 30% in 2000
- 2008 Crisis
  - Wiped out up to $8 trillion
    - $1,100 per person on the Earth
  - Trust across the world dropped
    - Austria lost 13% confidence
- Tobacco industry was viewed more favorably

Earning Trust: Ethics and Transparency

- Formalized standards of ethics
  - Not-industry wide
- Fiduciary standards
- Professional education requirements
  - Certified Financial Planner
  - ASU Oath of Honor
  - ACBSP mandated ethics learning
- Decentralize the firm
  - It is part of a network of stakeholders, not the central point
- Global regulation and oversight
- EU
  - EMIR/MiFIR/SFTR
- Clear and effective corporate communication

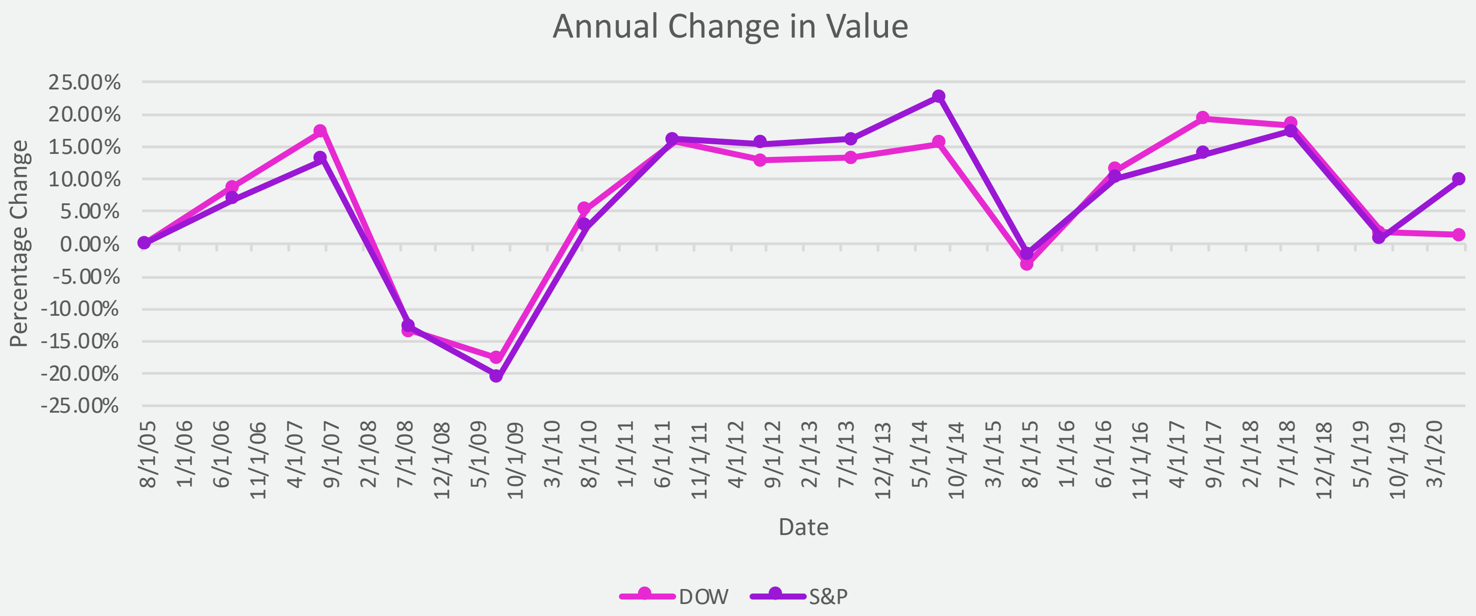
Shift in Strategies

- Hedge funds
  - Investors shifted toward lower volatility funds
- Banks tightened underwriting
- Venture capitalists focused on ’core sectors’
- Prior to 2008
  - Dutch life insurance firms (stablizers)
    - Acted in procyclical manner
      - Exaggerated market swings



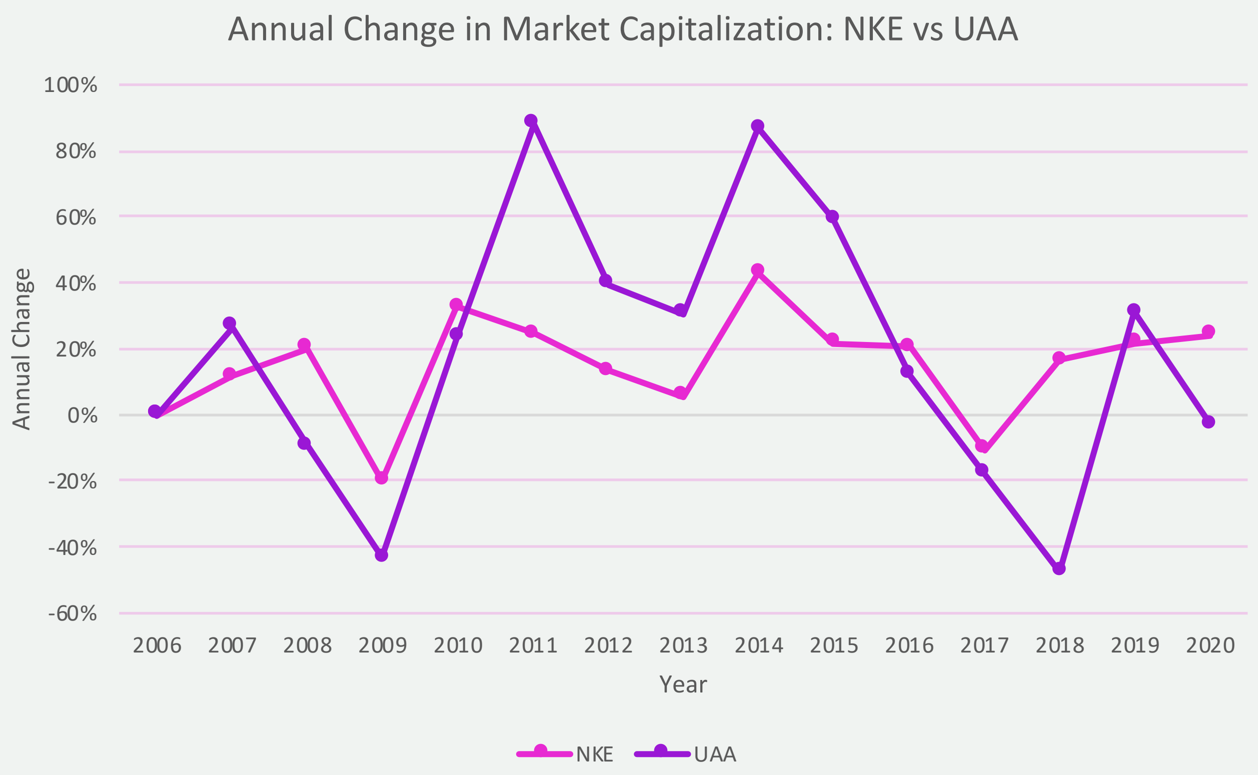
Risky VS Safe Investing

- DJIA considered safe
- S&P 500 considered risky
- Markets as a whole tend to move together
- DJIA had a slight advantage



Risky VS Safe Investing Pt. 2

- Focused on two firms
  - DJIA - NKE
  - S&P - UAA
- Greater changes in market cap for UAA



Conclusions

- Trust, ethics
  - Have become more important to a degree
    - Still work to be done
- Transparency
  - Most clear cut increase
    - Government regulation
    - Corporate communication
- Safer strategies?
  - Unclear due to lack of data
    - Firms do not typically disclose investment strategies
- Lots of talk, little action on a large scale

References

ACBSP. (2019). *ACBSP UNIFIED STANDARDS AND CRITERIA FOR DEMONSTRATING EXCELLENCE IN BUSINESS PROGRAMS*. Overland Park, Kansas: ACBSP.

Ahlstrom, D., Arregle, J., Hitt, M. A., Qian, G., Ma, X., & Faems, D. (2020). Managing Technological, Sociopolitical, and Institutional Change in the New Normal. Journal of Management Studies (John Wiley & Sons, Inc.), 57(3), 411–437. https://ezproxy.wagner.edu:2310/10.1111/joms.12569

Baker Library. (n.d.). Lehman Brothers Introduction. Retrieved July 22, 2020, from https://www.library.hbs.edu/hc/lehman/Exhibition/Introduction

Bernanke, B. S. (2010, January 3). Monetary Policy and the Housing Bubble. Retrieved July 23, 2020, from https://www.federalreserve.gov/newsevents/speech/bernanke20100103a.htm

Chen, J. (2020, April 19). Hedge Fund. Retrieved July 23, 2020, from https://www.investopedia.com/terms/h/hedgefund.asp

References

CFP Board. (2020). CFP® Certification: The Standard of Excellence. Retrieved July 22, 2020, from https://www.cfp.net/why-cfp-certification/the-standard-of-excellence

Conti, A., Dass, N., Di Lorenzo, F., & Graham, S. J. H. (2019). Venture capital investment strategies under financing constraints: Evidence from the 2008 financial crisis. Research Policy, 48(3), 799–812. https://ezproxy.wagner.edu:2310/10.1016/j.respol.2018.11.009

Dow Jones Industrial Average (^DJI) Historical Data. (2020, July 22). Retrieved July 22, 2020, from https://finance.yahoo.com/quote/^DJI/history?period1=1121385600

Duijm, P., & Steins Bisschop, S. (2018). Short-termism of long-term investors? The investment behaviour of Dutch insurance companies and pension funds. Applied Economics, 50(31), 3376–3387. https://ezproxy.wagner.edu:2310/10.1080/00036846.2017.1420898

ELLIOTT, R. C. (2013). Regaining Client Trust Requires Further Commitment by Wealth Managers. *Journal of Wealth Management*, *16*(1), 81–84. https://ezproxy.wagner.edu:2310/10.3905/jwm.2013.16.1.081

References

Fidelity Learning Center. (2020). What are mutual funds? Retrieved July 23, 2020, from https://www.fidelity.com/learning-center/investment-products/mutual-funds/what-are-mutual-funds

Fiduciary Responsibilities. (2020). Retrieved July 22, 2020, from https://www.dol.gov/general/topic/retirement/fiduciaryresp

Hayes, A. (2020, May 08). The Bernie Madoff Story. Retrieved July 22, 2020, from https://www.investopedia.com/terms/b/bernard-madoff.asp

Jardelot, J., & Mitov, M. (2015). The drivers behind the reporting obligations of EMIR, MiFIR and SFTR. *Journal of Securities Operations & Custody*, *7*(4), 348–354.

Kappel, M. (2019, April 03). Transparency In Business: 5 Ways To Build Trust. Retrieved July 24, 2020, from https://www.forbes.com/sites/mikekappel/2019/04/03/transparency-in-business-5-ways-to-build-trust/

References

Knell, M., & Stix, H. (2015). Trust in Banks during Normal and Crisis Times--Evidence fromSurvey Data. *Economica*, *82*, 995–1020. https://ezproxy.wagner.edu:2310/10.1111/ecca.12162

Mcconnell, J. J., & Buser, S. A. (2011). The Origins and Evolution of the Market for Mortgage-Backed Securities. Annual Review of Financial Economics, 3(173). doi:10.2139/ssrn.1840723

NIKE Market Cap 2006-2020: NKE. (2020). Retrieved July 22, 2020, from https://www.macrotrends.net/stocks/charts/NKE/nike/market-cap

ÖKTE, K. S. (2012). The Financial Crisis of 2008 in the Usa: An Overview. *Journal of the Faculty of Economics / Iktisat Fakültesi Mecmuasi*, *62*(1), 81–101.

Pajarskas, V., & Jočienė, A. (2014). Subprime Mortgage Crisis in the United States in 2007-2008: Causes and Consequences (Part I). *Ekonomika / Economics*, *93*(4), 85–118.

Pajarskas, V., & Jočienė, A. (2015). Subprime Mortgage Crisis in the United States in 2007-2008: Causes and Consequences (Part II). *Ekonomika / Economics*, *94*(1), 7–41. https://ezproxy.wagner.edu:2310/10.15388/Ekon.2015.1.5317

References

Shim, S., Serido, J., & Tang, C. (2013). After the global financial crash: Individual factors differentiating young adult consumers' trust in banks and financial institutions. *Journal of Retailing & Consumer Services*, *20*(1), 26–33. https://ezproxy.wagner.edu:2310/10.1016/j.jretconser.2012.10.001

S&P 500 (^GSPC) Charts, Data & News. (2020, July 22). Retrieved July 22, 2020, from https://finance.yahoo.com/quote/^GSPC?p=%5EGSPC

Tripp, E. (2015). How to Restore Public Trust in Banking. *Ivey Business Journal*, 1–4.

Twin, A. (2020, July 01). Business Ethics: Fair Business Policies Within Controversial Subjects. Retrieved July 24, 2020, from https://www.investopedia.com/terms/b/business-ethics.asp

Under Armour Market Cap 2006-2020: UAA. (n.d.). Retrieved July 22, 2020, from https://www.macrotrends.net/stocks/charts/UAA/under-armour/market-cap

US Bureau of Labor Statistics. (n.d.). Latest Benefits News Release. Retrieved July 22, 2020, from https://www.bls.gov/ncs/ebs/

Wang, Y., Watson, J., & Wickramanayake, J. (2018). The global financial crisis and the mutual fund flow–performance relationship. *World Economy*, *41*(11), 3172–3193. https://ezproxy.wagner.edu:2310/10.1111/twec.12673

WERHANE, P., HARTMAN, L., ARCHER, C., BEVAN, D., & CLARK, K. (2011). Trust after the Global Financial Meltdown. *Business & Society Review (00453609)*, *116*(4), 403–433. https://ezproxy.wagner.edu:2310/10.1111/j.1467-8594.2011.00391