

# The Crisis Predictor

05-01-2009 by [Lars Lønstrup](#) - Translated by *Jens Kjaer Soerensen*

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The interest only loans have already damaged our economy, but they are now again being sold in huge numbers. Only politicians can now change the development, says economist Jens Kjaer Soerensen, who in his thesis from March 2006 foresaw the financial crisis.

The young Danish economist Jens Kjaer Soerensen recently immigrated to Los Angeles, USA. He left a well paid job as an investment banker in a larger Nordic bank to be an entrepreneur in an American clean tech start-up.

A story by it self, but that will have to wait, because Jens Kjaer Soerensen had another story to tell DJOEF magazine before he left Denmark.

He wanted to warn about the fact that many house owners is in danger of entering serious economic difficulties in the coming years, and more so than the economic debate shows.

The reason is that interest only loans are now being sold in large numbers. The loans, which already has made the Danish house owners some of the most indebted in Europe, has once again become attractive due to the many interest rate cuts. But it is only a matter of time before the interest rate will increase again, and the risk of the increase being abrupt is present due to the current economic environment.

If such happens, the effect of increased monthly payments will hit the hundred thousands of Danes who have financed their homes with variable and interest only loans directly. For many people it would be the straight line to technical insolvency and the risk of foreclosure.

Yes, it is a scary perspective on the future, but isn't that a little hypothetically, some might say.

With such an approach you would take the same sceptical view as Jens was met with by censor when Jens Kjaer Soerensen three years ago was examined in his thesis. In this thesis, the at the time 27 year old student in Economics, foresaw a world spanning credit and financial crisis, caused by a 10-year (1993-2006) abnormal high return on houses in a number of connected western economies. The thesis also predicted that the financial crisis potentially could result in a global economic recession.

In March 2006 it was only relatively few economists – amongst others Robert J. Shiller and Jens Kjaer Soerensens own Professor Jakob Broechner Madsen – who had the overview of the conditions in the housing market. Therefore Jens had to fight in order to convince censor before he could leave the examination room as Master of Science in Economic.

### **A fighter with macro economic perspective**

But how on earth was a Danish economic student able to foresee how the world economy would develop an entire year before the American sub prime crisis initiated the crisis.

“Of course Jens is clever, but many people are regarded as such, if they are good at adjusting to what people want to hear. Jens has a drive towards what he believes in him self and then he is an incredible fighter”, the fellow student Morten Falch says.

The former professional soccer player in FCK is today working as a portfolio manager for a larger Danish bank, and he has known Jens Kjaer Soerensen, since they started at the studies at the University of Copenhagen in 2000.

They quickly got together and wrote assignments together, because they were interested in the stock market and could handle critique, if it was necessary to move on, explains Falch. And then we were a great supplement for each other.

While I am the micro type who analyze individual companies to find out whether they are worth investing in, then Jens is the macro type who is passionate about the greater picture of the economy. It gives funny and interesting conversations, and that’s the reason why we have seen each other after our studies.

### **Limited possibilities in the bank**

It was during the first years of his studying that Jens Kjaer Soerensen brought his interest of the stock market into a job in a greater Nordic bank. Shortly after his full time employment in the same place Jens Kjaer Soerensen arranged in the summer of 2006 seminars for his colleagues with his former professor and guide Jakob Broechner Madsen, who as the first in Denmark warned about the booming housing market.

The audience was listening quietly, but also asked very sceptical questions. At the time there was not much in their daily lives, which pointed in the direction that the professor was right in his predictions about coming great declines in housing prices. One of the macro analysts engaged more in the conversation than the others.

“He believed that the new loan types - in USA sub prime, and in Denmark interest only loans and variable loans – had driven house prices up to a permanent higher level. Broechner and I denied that, since all financial history has shown that real house prices would be constant in the very long run, Jens Kjaer Soerensen remembers.

In the month after he experienced that the seminar had initiated some new thoughts in the head of the analyst. But the market was in a face, where the interest of buying was enormous, whereas the analyst had difficulties in using his new knowledge.

“Experiencing such gave reason to think twice, and resulted that I didn’t express my opinions as loudly, since there was no demand for them.”

### **That sounds a little resigning?**

“Yes, but it was not as exiting. I was satisfied by serving the customers as optimal as possible – to execute their orders about buying and selling in the market and optimize our internal systems – but I have always wanted to analyze the greater economic relations and think one, two or maybe three steps ahead. This opportunity just never appeared in my job, and then you will have to find other ways.

### **Real Estate and the financial markets as a hobby**

Parallel with the job as an investment banker Jens Kjaer Soerensen build a web-page where he presented his research, partly his thesis, partly added analysis of the national and international real estate and financial market. He writes about interest rate cuts, which has been the central banks universal tool against a sign of an economic crisis.

“Right now the world economy is in the middle of an enormous experiment with extremely low interest rates and gigantic stimulus packages all over the world. It happens even though, all economists know that by stimulation the economy so greatly, will with high probability lead to inflation,” he explains and continues:

“If this happens, it will almost certainly lead to interest rate increases in most economic countries, including Denmark, because the European central bank, ECB has declared a goal to keep inflation constant. Therefore it is very risky, when we in Denmark are seeing an increase in the use of variable interest only loans. That was exactly what happened in the 2003-2006 which made house prices explode, and Danes increased their debt way too much.”

## **Politicians must regulate**

The ministry of economics and business who lead the initiatives behind interest only loans turned down the idea that interest only loans caused the house prices to increase as late as in October of 2008. The same does professor in economics Jan Rose Skaksen from Copenhagen Business School, who was one of the economic wise in the Economic Council who back in 2003 gave the green light to the new loan type.

“Interest only loans caused the housing prices to increase, but it was not the most important factor, because we experience similar increases in house price in other countries who don’t have the same financing methods for their market,” he sais.

Jan Rose Skaksen however, agree that the interest rate will increase and he is just like Jens Kjaer Soerensen critical towards the mortgage package, which the Ministry of Economics and Business together with the Financial Supervisory and Insurance and Pension implemented in October 2008, which in the days after led to substantial decreases in the short term interest rate.

“It was an additional signal to owners of real estate that you can safely take interest only loans with a variable profile, because if things go wrong, then we will be there to save you. You can fear that such a political action can make many home owners to jump on board the wagon,” says Jan Rose Skaksen.

The largest risk is that home owners with interest only loans will be in trouble in the coming years if banks haven’t made sufficient risk evaluations on their customers, he thinks.

No one wants to lend out money, if you are not sure to get them back. So if the banks do so, it is rather an adjustment of how risky a portfolio the banks can have, you will have to adjust, if you politically want to regulate the market for mortgage and other financial products,” sais Jan Rose Skaksen.

You have to remember that banks are relatively short sighted and that they are constantly under competitive pressure of loosing market share, “Jens Kjaer Soerensen says.

“When politicians act to prevent increases in the short term interest rate, as we saw it in October, then it is possible that the market adjust to the fact an implements an expectation that more real estate owners who has variable interest only loans, the greater the probability that the government will have to step in, if the home owners at a later stage head into problems.”

Jens Kjaer Soerensen suggests political regulation of the market for mortgages. This could be a maximum of how much an individual can finance through interest only and variable loans. The advantage of regulation is that it would benefit the individual loan taker, the economy as a whole and the financial sector, he points out.

### **American love and clean tech**

And now the time is set for America. Jens Kjaer Soerensens American wife is awaiting him, after she left him a half a year ago. She is a lawyer, and it was while she was an exchange student in Copenhagen that they met a couple of years ago.

### **Will you stay over there?**

"I don't know. The move is thought as relatively permanent, but if the right opportunity about a dream job as a macro analyst in a greater Danish or International economic organisation arise, where I would be able to work with the prevention against economic crisis as the one we are experiencing now, then I might convince my wife to move again."

But right now the reality is a role as a CFO, the responsible for financing, in an American start up company by the name of Earthlite. The founders have met Jens Kjaer Soerensen through friends friends, and they welcomed him in the circle after they had read his view on the market potential and his view on the future financial strategy.

The product is an energy efficiency system, which can reduce electricity consumption by up to 50-60%, and the target group to start with will be larger public buildings as schools, universities and libraries.

"Global warming is an enormous problem and with the current political will to do something about the problem, there is a great commercial potential for a company like ours. There is of course a lot of potential competitors in a market, which is in a thriving development, and that's why we have to move now. I hope that my contacts within the financial world can be an asset in our search for capital."

### **What will you live from?**

"I have some savings – for instance from an apartment I sold – and then my wife will help. I will definitely give it 6-12 months, but then we have to see some results. I am a young man, why not try?"