

NovaPro foresaw the financial crisis

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When Lehman Brothers filed for chapter 11 in September 2008, the global economy sank quickly, and the magnitude of the financial crisis came as a surprise for most people. One of the new members of NovaPro knew already 2.5 years before the financial crisis broke out, that something big was under way. He wrote a thesis about housing bubbles that busts.

It is rare that you have the opportunity to verify whether your thesis hold in praxis as well as in theory, in such a way as the NovaProfessional Jens Kjaer Soerensen. In 2006 he was about to finish his studies at the Institute of Economics at the University of Copenhagen and because of previously being alerted by the international house prices, the subject for the thesis was chosen as an analysis of busting bubbles in the real estate markets throughout the 20th century and the consequences hereof.

"I made an assignment in 2004 together with a fellow student about the housing market, and we realized, that many housing markets had the same trend, and already back then we concluded, that a bubble was being created. It was something relatively new at the time, and there was a lot of debate especially at the studies about the phenomenon. My thesis orientator was also sure, since he meant that this was the next big bubble, that you would see bust," explains Jens Kjaer Soerensen.

The thesis consisted of an analysis of 4 real estate markets– USA, England, Netherlands and Norway –, where the historic data regarding the parameters as rent, income and construction costs for new houses was analyzed as a foundation for the dynamics of house prices. And as the thesis progressed a clear pattern was discovered. 93% of former housing bubbles could be explained by, a boom in housing market initiated by deregulation.

The difference between the current housing bubble, which was created in the beginning of the 2000s, and the former was the magnitude of the deregulation, which had taken place in the mortgage markets resulting in creative loan types as interest only loans and break loan etc., which has become an extremely popular way for first time buyers to use when entering the real estate market.

Even though everyone has seen the size of current bubble, there is another little historic detail, which it is worth noticing.

"In the process we looked at the indebtedness of the population relative to GDP," he explains. "And since the beginning of the 20th century there has only been one prior time where there has been a threatening "gap" between the two. This was just after the Great Depression in 1929, where GDP started to decrease. But if you looked at the indebtedness at the time, when I wrote my thesis, it was already way higher many places in the world, than even after the Depression. Such a detail is a clear danger signal of the economy should and it should make every economist worry."

The conclusions from the thesis made Jens Kjaer Soerensen arrange some seminars at his former employer in the financial sector, which focused on the potential outlook for the economy. When the financial crisis finally came, Jens was as known confirmed by his prophecies, but was also surprised at how quick the development went.

"It is not quite pleasant to be witness to as an economist to be in first row of an economic meltdown, and that the exchanges almost collapsed around you. It was a surprise to everyone how fast it went," he ends.

The thesis focused on analysing the foundation of the internationally synchronized real estate bubble, but Jens Kjaer Soerensen is considering writing a book to follow up on the subject. The financial crisis has unfortunately not yet reached its maximum, so there will probably be plenty of material.