

# FINDING THE CAUSES OF FINANCIAL CRISES: THE HUMAN FACTOR



As a society we place a high priority from learning from our mistakes. Even relatively small-scale disasters are followed up by thorough investigations to determine what caused them. For example, the National Transportation Safety Board investigates every single accident involving a U.S. aircraft.<sup>1</sup>

One of the costliest disasters in recent history was the market crash of 2008. From its peak to the lowest point, The Dow Jones Industrial Average index dipped by a third of its value. The federal government responded by pumping hundreds of billions of dollars into a financial bailout plan designed to stave off a potential depression.<sup>2</sup>

In the years that followed, government officials, academics, and Wall Street experts have studied this financial crisis from every angle in an effort to understand why it happened, and to figure out ways to keep it from repeating.

While the basic facts about what caused the investment banks and insurance companies to start failing are not hard to ascertain (short answer: mortgage backed securities), what's more difficult is to determine why people who should have known better enabled the disaster to unfold.

Though the public wants answers right away, something as complex as the collapse of entire financial system requires more time to reflect back and identify the primary causes.

About a year ago, near the 10th anniversary of the 2008 crash, University of Pennsylvania's Wharton School of Business convened a conference in New York titled "Financial Markets, Volatility, and Crises: A Decade Later."<sup>3</sup>

As you can imagine, the panelists were not in agreement on everything related to the crisis. For example, they had a divergence of opinions on exactly when it started. But they did tend to

agree on some of the primary human factors involved.

Bruce Jacobs, co-founder of Jacobs Levy Equity Management, said that the crashes of 1987 and 2008 were both fueled by "free lunch strategies." He said that investors had an expectation of protection and safety, and at the same time the securities were sold to them on the basis of higher returns.

In other words, contrary to what global markets have evidenced for decades, people once again thought they could earn huge gains with virtually no risk.

Richard Lindsey, co-head of liquid alternatives at Windham Capital Management, said that crises often begin when a new product or approach is sold as a panacea to the risk/return trade-off. When neither the firms selling it or the investors buying it really understand the product, accurate risk assessment is almost impossible.

Vineer Bhansali, founder of LongTail Alpha investment advisory services and survivor of five financial crises, agreed. He said that the catalyst tends to be "a great theorem that goes bad because it's abused and levered up."

Unfortunately, Bhansali observed, investors tend to have a short memory. Once the crisis is over, confidence returns, and *investors start chasing returns again*.

The prudent investor should learn two things from this.

First, greater returns should always be expected to carry greater risk—there's no such thing as a free lunch.

Second, significant market volatility, including full blown financial crises, should not come as a surprise. In fact, you should prepare for them both emotionally and in your long-term investing strategy.

Maintaining a healthy emotional outlook and a prudently-diversified strategy are fundamental to helping you endure the unknown future as an investor in global markets. We can help ensure that you maintain a proper perspective on your journey toward your ideal financial outcomes.

Have a great weekend!

## Golf Tip of the Week

**Want a Longer, Cleaner Drive? Grab a Towel.**



Unlike most of the clubs which require a downward hit on the ball for good contact, the driver requires an upward strike. Unfortunately, most amateur golfers do the opposite, catching the ball when the club is still moving downward – leading to pop-ups and less-than-impressive distance. This might sound a little strange, but this is when you go grab a towel.

This isn't a new tip, but it is an effective one. Next time you're practicing your tee shots, take a rolled-up towel and place it a few inches in front of the ball. As you try to avoid the towel, your body will naturally hit higher "up" on the ball.

Changing your angle of attack in this way will create optimal launch conditions for a truly awe-inspiring drive.

Tip courtesy of Alison Curdt, PGA | Golf Tips Magazine<sup>1</sup>

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## Recipe of the Week

### Fresh-Squeezed Lemon Cake



Yield: 2 (8-inch) loaves

## **Ingredients:**

2 sticks unsalted butter, use at room temperature  
2½ cups granulated sugar, divided  
4 extra-large eggs, use at room temperature  
⅓ cup grated lemon zest (6 to 8 lemons)  
3 cups flour  
½ tsp. baking powder  
½ tsp. baking soda  
1 tsp. kosher salt  
¾ cup freshly squeezed lemon juice, divided  
¾ cup buttermilk, use at room temperature  
1 tsp. pure vanilla extract

## **For the glaze**

2 cups confectioners' sugar, sifted  
3½ Tbsp. freshly squeezed lemon juice

## **Directions:**

### **Cake**

1. Heat your oven to 350°F. Grease and flour 2 (8½" x 4¼" x 2½") loaf pans.
2. In the bowl of an electric mixer, using the paddle attachment, cream the butter and 2 cups of sugar, about 5 minutes. You want a fluffy texture. Add the eggs, one at a time, mixing on medium speed, and then, add the lemon zest.
3. Sift the flour, baking powder, baking soda, and salt in a bowl. Combine ¼ cup lemon juice, the buttermilk, and vanilla in a separate bowl. Alternate adding the flour and buttermilk mixtures to the batter in the mixing bowl. Once combined, pour the final batter evenly into the 2 pans and bake for 45 minutes to 1 hour, until a toothpick comes out clean.

### **Syrup**

1. Put ½ cup granulated sugar with ½ cup lemon juice into a small saucepan. Simmer over low heat until the sugar dissolves.
2. Remove syrup from heat.
3. Cool the cakes for 10 minutes, then turn them out on a sheet pan.
4. Spoon the lemon syrup over them. Allow the cakes to cool completely.

## Glaze

1. Whisk the confectioners' sugar and lemon juice together in a bowl until smooth.
2. Glaze the cakes, drizzling the topping down the sides.

Recipe adapted from Food Network<sup>ii</sup>

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## Health Tip of the Week



### Intermittent Fasting Benefits

Giving yourself a fasting period each day, plus a limited window of time that you do eat, may be seriously beneficial to your health. Intermittent fasting involves time periods in which you eat and alternating ones in which you don't. For example, if you have your last meal of the day at 5 pm, and you don't eat until 9 am the next day, that is a 16-hour cycle of fasting and an 8-hour cycle of eating. Here are some evidence-based benefits:

#### Weight loss

You'll eat fewer meals, take in fewer calories, enhance hormone function, and reduce insulin levels to more efficiently use fat for energy. Your metabolic rate can increase too.

#### Reduction in blood sugar levels

Intermittent fasting may reduce fasting blood sugar and protect against kidney damage.

#### Resistance to oxidative stress

Studies have shown that intermittent fasting can enhance the body's resistance to the oxidative stress that could lead to aging and chronic disease.

Tip adapted from Healthline<sup>iii</sup>

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**Our mailing address is:**

Ballentine Capital Advisors  
23 Buena Vista Way, Suite B  
Greenville, SC 29615

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Sources:

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<sup>i</sup> <https://www.golftipsmag.com/instruction/driving/try-towel-drill-for-longer-drives/>

<sup>ii</sup> <https://www.foodnetwork.com/recipes/ina-garten/lemon-cake-recipe-1913110>

<sup>iii</sup> <https://www.healthline.com/nutrition/10-health-benefits-of-intermittent-fasting#section1>