ASX

Schools Sharemarket Game

BOOMS & BUSTS

Supplementary lesson 4

Includes: Student lessons . Teacher notes & answers

History of the Sharemarket: Booms & busts

Introduction:

The purpose of this unit is to introduce students to some of the history of the sharemarket, along with gaining an understanding of economic cycles, particularly the pattern of strong markets being followed by periods of weakness.

Some of the most dramatic market events are covered in detail including the psychology of investors and the notion of greed and fear as drivers of investor behaviour.

The videos should maintain student interest. This unit does go into more depth on economic matters than other units.

Lesson Design:

Online lesson

Expected Learning Outcomes:

Students will:

1) Gain a better understanding of how markets move in cycles
2) Learn more about the history of sharemarket booms and busts
3) Gain some awareness of the role of psychology in investor behaviour

Overview of Student Lesson:

1) Read the introduction: **'Booms and busts'** (pg S.1).
2) Either watch as a class or ask students to watch the YouTube videos and answer questions.

   There are 3 videos for students to watch:

   a) 1929 Stock market crash (pg S.1)

   b) 1987 crash – first 6 minutes (pg S.3)

   c) Dot Coms Gone Bust USA (pg. S.4)

3) Read Global Financial Crisis & Booms (pg S.6 – S.7) and discuss how markets move in cycles, how booms and busts affect people and at what stage of the cycle do students think the sharemarket might be currently?
4) **'Investigate':** Students are encouraged to talk with their parents and grandparents about their experiences of the sharemarket crash of 1987 and the global financial crisis (pg. S.8).

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Teacher Notes: BOOMS & BUSTS

Video 1: Wall Street Crash of 1929

Overview: Prior to the 1929 crash, there was a period of strong economic growth. Many ordinary people started putting their money into a booming stock market. Speculation was common. This meant that people were buying shares solely in the hope of making a quick profit rather than investing based on the fundamentals of companies. People were borrowing money to invest and if the market fell the banks would ask for additional funds.

When the markets began to falter, investors started to panic and sold their shares trying to rescue disappearing profits. Those who had bought shares on margin were forced to sell. All this caused prices to spiral downwards.

Black Thursday – 24 October saw shares drop by 13%. Some bankers on Wall Street tried to lift the market and bring back confidence by buying as many shares as possible, however it only worked for a short time, and then there was…

Black Tuesday – 29 October and the US markets lost another 12%. Thirty billion dollars was lost in the US alone and it took twenty-five years for the Dow Jones to recover to pre 1929 levels.

The Great Depression followed the stock market crash. The Great Depression resulted in many people around the world being unemployed. Incomes fell, international trade was decimated and the price of just about everything plummeted. It took 12 years to recover.

The connection between the stock market crash and the Great Depression is argued by economists. Some see it simply as part of an economic cycle of boom and bust. But it is fair to say that the banks were actively involved in all aspects of economic life, including the stock market. The crash resulted in a loss of confidence generally and considerably weakened the banks that did survive the crisis.

Answers:

1) **In the 1920's was it prosperous? Which areas in America were the most prosperous?** Yes, very prosperous, especially in the cities.
2) **Where were people making the most money?** People were making fortunes in the stock market.
3) **What was happening to the economy in the summer of 1929?** In the summer of 1929, unemployment was rising, automobile sales and department store revenues fell sharply and farms were failing, *but on Wall Street – people were still very optimistic.*

   On 27 August 1929 the stock market reached its peak – buyers kept buying as they didn't want to miss out. They camped out so they could buy shares.
4) **Were there warnings that the boom times might be coming to a close? Did people take notice?** There was a warning given by an economist that a crash was coming, but most didn't listen. However, the mood started to change and investors became uneasy.

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5) **What happened on Wednesday 23 October 1929?** The first wave of panic selling started. The next morning there was more panic, share prices plummeted and in less than 2 hours 10 billion dollars was wiped out.
6) **Why were people shocked? What did they do?** Investors stood around, shocked, dazed, and couldn't believe that it was happening.
7) **What did the bankers agree to do? Did it work?** They pumped millions of dollars into the market to stop the fall in share prices. People thought the market had been saved. However, on the Friday – with stock market prices stabilised, banks withdrew funds. The banks had been badly affected by investing in the market themselves and also by lending to people who had invested in the market. Many of these people could no longer afford to repay their loans.

   The actions of the banks caused investors, who were already very nervous, to panic.
8) **Tuesday 29 October 1929 – what is this day known as? What happened?** This day is known as Black Tuesday. There was another wave of selling and this time no one came to the rescue. The stock market was in chaos. People panicked and were prepared to sell their shares at any price. 16 million shares were traded and the market lost 14 billion dollars – an overall total of 30 billion dollars was lost in just one week.
9) **Who was the worst hit? How much did they lose?** Small investors were the worst hit, as many had margin loans and most were wiped out, losing everything - houses, life savings, etc.
10) **What did those with money do?** They bought shares in huge quantities with the expectation of profiting once the market recovered.
11) **How long did it take for the American economy to recover?** Ten years. In other countries it took much longer.

Video 2: The Crash of 1987 – watch to 6.25 minutes

Overview: **Black Monday** – From the early eighties to 1987 stock markets around the world experienced strong growth. People who invested in the stock market were rewarded with soaring gains. In Australia, the market was at record levels in 1987 - the All Ordinaries index rose by 381% in 5 years, which is an increase of nearly 4 times over the period.

On 19 October 1987, the world stock markets experienced their largest one-day crash in history. The falls occurred on all financial markets. The Dow Jones lost 22.6% of its value in one day, around US$500 billion. The Australian sharemarket lost around 25% that day and 41.8% of its value by the end of October.

The exact cause of the crash remains unknown; however the first market to fall was Hong Kong, where stock market speculation had been widespread. Other markets soon followed. This was due to a range of factors including modern communications whereby news travelled much faster, as well as global investment being more wide spread. This meant that events on one market could have an effect on investors who were also investing in other markets..

In America, computerised trading was also considered to have added to the problem. This type of trading involved computer generated orders being triggered in certain market conditions. It is believed that very large orders were filled in a very short period of time which added to market panic and confusion.

Another factor was that people who had borrowed money to invest in the stock market owed money once prices fell. Many had to sell their shares to pay their margins and this caused prices to fall further.

Unlike the crash of 1929, the markets quickly recovered helped in part by government measures which were intended to help stimulate the economy. The Dow Jones Industrial Average ended the year on a level higher than it had started.

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Answers:

1) **What was this day called in America?** Black Monday
2) **What happened?** The market panicked. The Dow dropped over 500 points – approx 22% lost in one day.
3) **How did brokers react?** Stunned, shocked by how quickly it happened.
4) **How much did the Australian market fall on, 20 October 1987?** The Australian market lost around 25% of its value on 20 October and 41% of its value by the end of October.
5) **What was this day called in Australia & New Zealand? Why was it different?** In the US this event is referred to as Black Monday but in Australia and New Zealand it is called Black Tuesday due to the time difference. By the time markets opened in Australia there had been a massive sell-off around the world and Australian investors knew that markets here would also plunge.

Video 3: The Dot Com Bubble

1) **What pushed investors to pay significantly more for dot com stocks than their value?** Competition and speculation
2) **Name 3 companies that saw uprecedented growth?** Amazon, Ebay, Pets.com, GEO city
3) **The Nasdaq in 1995 was at 1000 points, where was it by the year 2000?** 5000 points
4) **What created the market bubble? The difference between perceived and actual value.**

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Student Lesson: BOOMS & BUSTS

Booms & busts

Markets tend to move in cycles – this means there will be times when the markets are up and the economy is booming, there are plenty of jobs, people are making money, they spend more money and max out their credit cards. It feels like the good times are just going to go on forever.

Some commentators say the sharemarket is driven by greed and fear. In the boom times, confidence is high and no-one wants to miss out on profits. Investors can sometimes get carried away in their optimism, borrowing a lot of money to invest, investing in risky companies and ignoring warning signs.

There will also be times when the markets are down, the economy is flat, there are fewer jobs around, less people are spending money and the cost of living is higher. People are worried about keeping their jobs and are not confident about the future. When people lose confidence, fear takes over. People become scared that they will not only lose the profits they have made but possibly all of the money they started with. Fear overtakes greed and people start to panic trying to sell their shares at whatever price they can get.

If you take a look back in history you can clearly see these cycles.

These are sometimes called booms and busts – a boom is where the market moves upward and continues to move up, and then there is a sharp drop which is often called a bust – this is when people can lose a lot of money.

In this lesson we will take a look at four major events that have had an impact on the market. Prior to each one of these events there was a boom time, where things were good, people were investing and making a lot of money.

THE WALL STREET CRASH OF 1929

Watch: **'1929 Wall Street Stock Market Crash'** and answer the questions below.
http://www.youtube.com/watch?v=RJpLMvgUXe8

1) In the 1920's was it prosperous? Which areas in America were the most prosperous?

2) Where were people making the most money?

3) What was happening to the economy in the summer of 1929?

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4) Were there warnings that the boom times might be coming to a close? Did people take notice?

5) What happened on Wednesday 23 October 1929?

6) Why were people shocked? What did they do?

7) What did the bankers agree to do? Did it work?

8) Tuesday 29 October 1929 – what is this day known as? What happened?

9) Who was the worst hit? How much did they lose?

10) What did those that had money do?

11) How long did it take for the American economy to recover?

Following this period from 1929-1932 there was a depression – this is known as **'The Great Depression.'** During this period, many people around the world were unemployed, incomes fell, international trade declined and the price of everything plummeted. It took many years for the economy to recover.

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The crash of 1987

Stock markets around the world, including Australia enjoyed strong gains for quite a period. People who invested in shares were rewarded with big profits. The low point was in July 1982 and the market peaked in September 1987. The All Ordinaries index rose by 381% in 5 years.

On Monday 19 October 1987, the Hong Kong stock market was the first to experience a big drop which then spread to other markets around the world, including Australia.

Watch: **'Black Monday – Part 1: Nightly Business Report – 19 October 1987** and answer the questions below. (Only watch to 6:25) http://www.youtube.com/watch?v=4pjSIlkNxXg

1) What was this day called in America?

2) What happened to the Dow Jones Index – how much did it drop on 19 October 1987?

3) How did brokers react?

(Continued over)

See if you can find out the following:

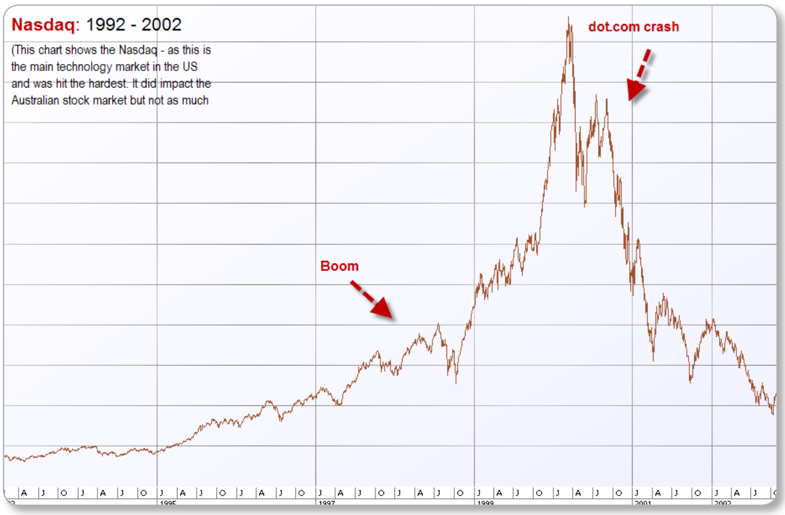
4) How far did the Australian sharemarket fall on 20 October 1987?

5) What was this day called in Australia & New Zealand? Why was it different?

The dot.com bubble

By the late 1990's, dot.com stocks (internet / technology) boomed as investors began buying up shares in companies that were built on promises based around new technology. Some talked about a new economy where profits didn't matter because it was all about growth and creativity.

While some companies became established, successful companies others didn't survive. During the dot.com boom many people speculated heavily, investing in any companies seen to be "high tech" or associated with the internet regardless of how these companies were performing.



Due to a slowing economy and concerns about continued losses people started to lose faith in the "dot.com story". In 2000, there was a massive sell off of these types of companies. Many investors and firms lost money and a lot of the dot.com companies went out of business.

Watch: **The Dot Com Bubble** and answer the questions on pg. S.5
https://youtu.be/I85ZmEdGLNM

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1) What pushed investors to pay significantly more for dot com stocks than their value?

2) Name 3 companies that saw uprecedented growth during this time.

3) The Nasdaq in 1995 was at 1000 points, where was it by the year 2000.

4) What created the market bubble?

5) Do you think this could happen again?

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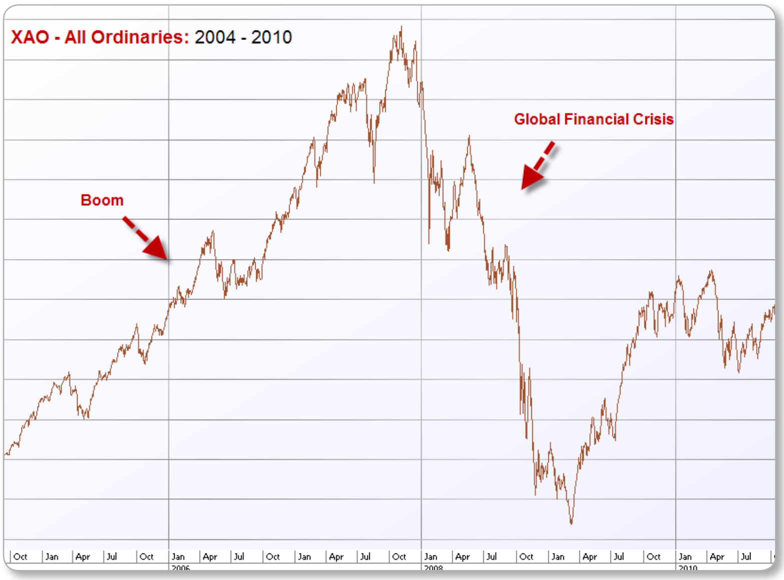
The global financial crisis (GFC) and the credit crunch



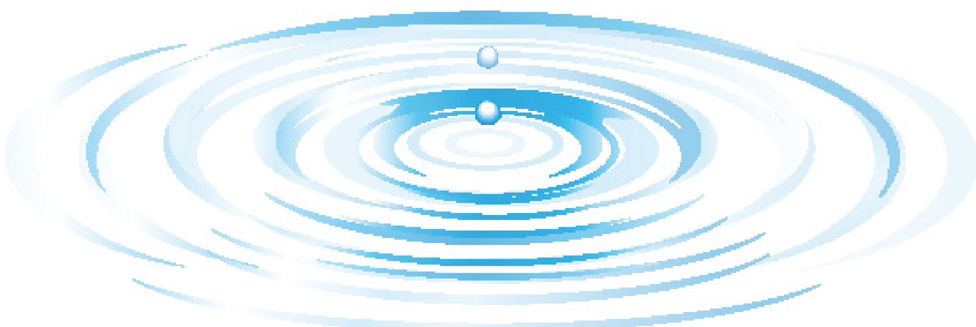
From 2001 to 2007 the sharemarket again enjoyed good times.

In America, banks were lending aggressively and property prices were skyrocketing. People could borrow a lot of money without necessarily being able to repay the money. Financial products were becoming more and more complicated and companies in the finance sector seemed to all depend on each other. If one big company had problems this affected a
lot of other companies as well.

People took on too much debt and were unable to repay their loans. This affected the banks and other lenders. Then those companies lending to the banks had problems and there was a worry that not just a few banks would collapse but the whole financial system.

If you throw a stone into a pond you can see the ripples spread out. Just like the stone in the pond, financial uncertainty caused the ripples that resulted in a massive loss of confidence in the American property market, in American banks and the stock market. These ripples then spread to other countries.

In 2008, the Dow Jones lost almost 34% of its value, its worst year since 1931 and the Australian market lost 41.3% for the year.



Booms: As you can see from the previous charts, prior to every one of these busts there was a boom time.

Discuss

1) When the market is booming how do people feel?

2) What are the advantages are of a market boom?

3) What might the dangers be?

So there you have it – some of the booms and busts over the past 80 years. One positive thing we can see from looking at the long-term performance of the sharemarket is that despite the busts, the market eventually recovers and booms again.

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Student Lesson: BOOMS & BUSTS

Investigate:

1) Ask you parents or grandparents if they remember 1987 and what happened?

   Did it affect them?

2) Did the GFC have an impact on their finances?

3) What lessons have they learnt from these experiences?

Notes:

Notes: