



The banking crisis: cause and effect

The first domino: Northern Rock

Narrator

In early 2007, the unravelling of sub prime and securitization set an economic firestorm raging throughout world markets.

Banks, institutional investors, and private homeowners – nobody was left untouched.

The first major victim in the UK was the Northern Rock Bank – and at the time, it seemed an isolated case.

News at Ten Archive sync

Tonight at Ten, Northern Rock appeals for calm and urges its customers not to panic.

News at One archive

Crisis at Northern Rock. Customers queue outside some of the bank's branches but the chancellor says it's a sound business.

News at Ten Archive sync

The decision by Northern Rock to seek emergency funding from the Bank of England marked it as the first high profile casualty of crisis in the international money market triggered by bad loans in the US housing sector.

News at Ten archive

Way past normal closing time on a Friday night. The Harrow branch of Northern Rock still open this evening dealing with queues of people waiting to withdraw their money.

When you've got your life savings invested you want to be sure they're safe don't you.

Well if they're not in trouble why are they having to borrow from the government.

Narrator

Banks lend money to one another in the interbank wholesale markets, but Northern Rock was more reliant than most on the funds provided by securitization, and was therefore more exposed when things started to go wrong.

David Llewellyn

"Northern Rock is a classic case study in what can go wrong when you exaggerate the significance of financial innovation, when you exaggerate the extent to which financial instruments can shift risk away from the bank onto others."

Narrator

The bank was no longer offloading its risks, but was buying into more and more of them.

Tetsuya Iskhikawa

You don't have a true transfer of risk; you actually have risk which is kind of beginning to feed itself, it's kind of going around in a circle."

Lord Skidelsky

"We cannot control risk. No. It is a myth. Keynes called it one of those pretty polite techniques that we use to lull our disquiet to the fact that we don't know what the future's going to bring."

Narrator

In the 12 months following the collapse of Northern Rock, things would get much worse.

News Archive of Lehmans, HBOS, RBS, B&B

Lehman Brothers has filed for bankruptcy after billion pound losses mostly in US....
....terrible death its like a massive earthquake.....on Sunday September 14th 2008 Dick Fould watched his company collapse..... 5000 staff at Lehman Brother's London office had no work to do except look for another job and get ready to move.

Vince Cable

"Following the Lehman Brothers collapse we had contagion throughout the whole system; confidence dried up in banks. We got to a point one evening when banks would no longer lend to each other overnight.

And that is the final collapse of confidence.

Narrator

Systemic risk – the idea of ALL banks collapsing - was looking more and more possible by the day.

Phillip Booth

"If a clearing bank actually becomes insolvent or there are serious worries about it becoming insolvent then we have a problem which can have systemic ramifications, because all banks are connected to each other, rather like all parts of a plumbing system are connected to each other.

People stop accepting cheques or debit card payments, or whatever it might be, and we all have to go back to using cash, and essentially the whole banking system can collapse because of the failure of one significant piece.

Vince Cable

"What has happened in this recession which is different from others is that, because of the crisis in the banking system, the banks are lending less, or are much more reluctant to lend, even to very good companies that have good order books, good profit records. They're tightening up their conditions. They are taking less risk."

Ken Jones

"Everybody out there who has worked for a living is wondering what the hell is going on, because we had a full order book and, bang - it's gone.

Orders stopped instantly.

Within a week we've run out of work from having seven to eight weeks worth of work in front of us all year and I made 85% of my workforce redundant. It's not very pleasant making somebody redundant just before Christmas. The look on their faces doesn't make you feel too good.

Ken Jones

"Everyday life has been affected now.
When you try to go to the bank now, and say,
'I'd like £25,000 as an overdraft.'
It's a definite no, no, unless you've got security.
My house. And I'm not letting them have that.
No way.

The last thing I want to do is put my house up as security and then lose it in a year's time and then be homeless as well as jobless.
That's the last thing I want to do."