**The Big Short**

**Introduction**

The Big Short is a movie based on the true story of the crashing of America’s housing market in 2007. This caused a lot of people to lose their employment and had impact worldwide. The whole movie revolves mainly around three people Michael Burry, Mark Baum and Jared Vennet. Michael Burry, a hedge fund manager, was one of the first person to get to know about the fact that the housing market might collapse which was at time very stable and strong. Jared Vennet was a trader in Deutsche Bank and he also gets to know about the upcoming crash of the market and tries to make profit from it and eventually does so. Michael Baum was also a fund manager and along with his team he dives deep into the market and finds the loophole but eventually also gets to know the intensity of it and how it may affect the lives of poor people.

**Concepts and Terms that I learnt**

So from the synopsis of the movie we may get to know that there are many terms related to finance in this movie. So I have listed out a few financial concepts and terms that I found out in the movie.

Treasury Bonds:

Treasury bonds, often referred to as T-bonds, are long-term loans made to the U.S. government. They are a type of government bond and are considered one of the safest investments because they are backed by the trust of the U.S. government. Treasury bonds have maturities of 20 or 30 years. So in simple words, when you buy a Treasury bond, you’re essentially lending money to the federal government. In return, the government agrees to pay you a fixed rate of interest every six months for the life of the bond. When the bond matures in 20 or 30 years the government pays back the original amount of the loan, also known as the bond’s face value.

Utility Stocks:

Utility stocks represent shares of companies in the utility sector, which provide essential services like electricity, water, natural gas, and telecommunications. Since these companies have particularly very low risk of performing bad hence the investment in these stocks are safer and reliable.

Bonds:

A bond is simply a loan taken by a company. Instead of going to a bank, the company gets the money from investors who buy its bonds. Companies give coupons to the investors. Coupons is simply a percentage of face value given as an interest to the investors by the company. When the bond of the contract terminates the company return the face value or principle value to the investors.

Mortgage Backed Securities:

Mortgage-backed securities (MBS) are investments like bonds. Each MBS consists of a bundle of home loans and other real estate debt bought from the banks that issued them. Investors in mortgage-backed securities receive periodic payments like bond coupon payments.

Credit Default Swaps (CDS):

A credit default swap (CDS) is a financial derivative that allows an investor to swap or offset their credit risk with that of another investor. To swap the risk of default, the lender buys a CDS from another investor who agrees to reimburse them if the borrower defaults.

Suppose a company sells a bond to an investor. Now if the debt issuer cannot guarantee that the company will be able to repay the premium, the investor assumes the risk. The debt buyer can purchase a CDS to transfer the risk to another investor, who agrees to pay them in the event the debt issuer defaults on its obligation.

FICO Score:

A FICO score, created by the Fair Isaac Corporation (FICO), is a type of credit score based on information in a borrower's credit report that lenders use to assess credit risk and determine whether to extend credit. In short, FICO score is used to determine the creditworthiness of the client.

FICO Score ranges from 300-850.

**300–579**: Poor

**580–669**: Fair

**670–739**: Good

**740–799**: Very Good

**800–850**: Exceptional

Subprime:

Subprime refers to a category of borrowers that carry higher risk compared to "prime" borrowers or loans. Subprime typically applies to individuals with lower credit scores or those who have a history of financial difficulties. Because subprime borrowers are considered riskier than the average borrower, subprime loans are subject to higher than average interest rates.

Collateralized debt obligations (CDOs):

A CDO is a financial product that pools together various types of debt, such as mortgages, bonds, or loans, and divides them into tranches sold to investors. Each tranche offers a different level of risk and return, with senior tranches being the least risky, allowing investors to choose the exposure that best fits their strategy.

Synthetic CDOs:

There are different types of CDOs and one of them is Synthetic CDO. It is structured with non-cash derivatives such as swaps, options, and insurance contracts. Synthetic CDOs are divided into tranches based on the risk assumed by investors. The value of a synthetic CDO is the cash flow derived from swaps, options, and insurance contract premiums (from, e.g., credit default swaps). And obviously senior tranches have lower risk and offer lower returns, while junior, equity-level tranches carry higher risk and offer higher returns.

ISDA Agreement:

An ISDA master agreement is a standard document regularly used to govern over-the-counter derivatives transactions. Over-the-counter (OTC) derivative transactions are financial contracts that are privately negotiated and traded directly between two parties, rather than being traded on an exchange. It is published by International Swaps and Derivatives Association.

Initial Public Offering (IPO):

An initial public offering (IPO) refers to the process of offering shares of a private corporation to the public in a new stock issuance. IPOs provide companies with an opportunity to obtain capital by offering shares through the primary market. An IPO is a big step for a company as it provides the company with access to raising a lot of money. This gives the company a greater ability to grow and expand.

Hedge Fund:

A hedge fund is a pooled investment that typically caters to institutional investors and uses a wide range of strategies to generate high returns. Unlike mutual funds or traditional investment funds, hedge funds are more flexible and have fewer regulatory constraints, making them riskier and allowing more complex investment strategies. Hedge funds typically target wealthy investors. Hedge funds play a critical role in providing liquidity to markets and helping to correct pricing inefficiencies.

SEC:

The U.S. Securities and Exchange Commission is an independent agency of the U.S. Government which creates laws against market manipulation. It was made after the Wall Street Crash in 1929. The SEC plays a crucial role in ensuring that securities markets operate transparently and that investors have access to accurate and timely information.

Shorting a fund:

This term was used many time in the whole movie. Shorting a Fund or Short Selling is a trading strategy in whicha trader aims to profit from a decline in a security's price by borrowing shares and selling them, hoping the stock price will then fall, enabling them to purchase the shares back for less money.

For example, an investor thinks that a company’s share value is going to fall. So it will buy the company’s share (Let’s say the price of share is 100 Rs and investor buys 100 shares) and when the company’s share falls it will buy them back again at lower price and get the remaining profit (Let’s say the price falls to 90 Rs, so the investor will by those 100 shares now at just 9000 Rs and hence make a profit of 1000 Rs).

**Conclusion:**

So these were all the financial terminologies and concepts that I learnt from this movie. I also got to know a housing market crash took place in America. And overall it was a great assignment to start my financial journey with.

**-Ojas Bajpai**