[Name of the Writer]

[Name of Instructor]

[Subject]

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The Warning

The documentary is an introspective look into the 2008 financial crisis and how it unfolded apart from the stock market crash. The documentary revolves around four people whose ideologies of the financial markets differ. Alan Greenspan, Robert Rubin and Larry Summers believe in a wholly unregulated market – a true Laissez-Faire economy - without any government intervention as Greenspan, a venerated economist, believes that markets correct themselves. Brooksley Born, a Stanford Law graduate and distinguished derivatives lawyer, believes in regulation to a certain extent in order to bring balance and stability in the market. Greenspan’s model dominates Washington and together with Summers and Rubin, the three are dubbed “The Committee To Save The World” by Time magazine. Meanwhile, Born, appointed CFTC (Commodities Future Trading Commission) Chairwoman, realizes the existence of a completely unregulated and huge market of derivatives, complex financial instruments, that has remained hidden from the US government. There is very little information about these transactions and even less about the people and organizations making these transactions. It was only because Proctor & Gamble filed a case, that the government came to know about the existence of this huge market that had the potential to destroy the whole economy. Born was worried that this would produce a domino effect if the 27 trillion dollar derivatives market and the big banks involved in it faced a crisis. She prepared a document called Concept Release, a set of regulations on over-the-counter (OTD) derivatives and this upsets Rubin. He calls an emergency meeting of the President’s Working Group, a secretive committee of President Clinton’s top financial advisors and office-bearers including Greenspan, Born and Summers. Greenspan and Rubin vehemently oppose Born and warn her to step back from her regulatory quest as it will endanger the entire economy. Witnessing the resolve of Born, Rubin writes to Congress and asks them to use whatever means necessary to stop the publication of Concept Release. A series of Congress hearings take place in which all financial advisors to government and top economists disagree with Born. This leads Congressmen to block Concept Release.

However, clouds of a crisis began to appear. Long Term Capital Management, a hedge fund management firm with Nobel Prize winning economists in the lead, has hundreds of billions of dollars in investment from various investors and they guarantee huge returns. However, their bubble bursts and they cannot pay off their liabilities, leading to a banking crisis. Rubin and Greenspan began making calls and urge banks to help in steering away the crisis. 14 big banks pledge billions of dollars to help stave off the crisis; it works and the crisis is averted. CFTC is stripped of its regulatory powers and Born resigns as a result.

A decade later, a serious crisis becomes imminent when stock market crashes in 2008. The warning of Born turned out to be prophecy that would result in losses of hundreds of billions of dollars and a global financial meltdown – all because of the absence of regulation. Later on, the crisis appeared to have taught a lesson and President Obama announced he would be regulating the derivatives market but the financial lobby spoke against it and got it delayed. Towards the end of the documentary, Born cautions that other crises will follow if regulations are not put in place.

The documentary shows that market is not capable of correcting itself if the investments in market become too volatile and their value gets high. The 2008 financial crisis teaches that true Laissez-Faire economy is not as rosy as some economists contend. The effects of zero regulation can be far reaching and disastrous for the economy. Capital starts to accumulate in derivatives which are extremely hard to understand for people so they become concerned with returns only. This leads to a race for numbers like LTCM did for many years for its investors. They secretly invested and made questionably high profits for their clients which urged further investment. However, the places to invest began to shrink and LTCM found it difficult to return profits so they went bankrupt. This would have been avoided if the government had let Born continue with Concept Release and regulated the huge derivatives market.

The documentary also shows the impact of blindly following economic theory. An economist of Greenspan’s caliber should have seen the writing on the wall but his insistence on following the Laissez-Faire system led to the devastating crisis of 2008. Another important takeaway is that speculation in open market leads to a bubble that is going to burst inevitably. Unfortunately, the period before the crisis is always one of consistent and remarkable financial growth. The 2008 crisis was preceded by phenomenal growth and profits in the stock market. The speculation led to further investments but returns began to diminish and this led to mass selling which drastically reduced prices of stocks.

Perfectly Competitive Equilibrium model takes into account the whole market as homogeneous with each seller and buyer insignificant in determining price as their contribution is too small to make a difference in prices. This model predicts the equilibrium price but it significantly differs from ground realities. The same calculation would have been done by Greenspan, Rubin and their teams but they would not have contemplated the differences in real life. In reality, the 2008 financial crisis had huge market players capable of influencing prices as well as market dynamics. Moreover, a lack of regulation served to embolden investors into making riskier investments that threatened the overall market stability. Once these investments failed to bring the expected returns, investors started to cash out which created a liquidity crisis, forcing LTCM to file for bankruptcy.

Works Cited

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