Business Finance II – 515 - summer 2016

Book Review – Write Up

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Book Title	Inside Job
Author(s)	Charles Ferguson
Publisher &Publishing Year	2010, Sony Pictures

Author (s):

In 1994, Ferguson founded Vermeer Technologies, one of the earliest Internet software companies, with Randy Forgaard. Vermeer created the first visual website development tool, FrontPage. In early 1996, Ferguson sold Vermeer for $133 million to Microsoft, which integrated FrontPage into Microsoft Office.

After selling Vermeer, Ferguson returned to research and writing. He was a visiting scholar and lecturer for several years at MIT and Berkeley, and for three years was a Senior Fellow at the Brookings Institution in Washington DC. Ferguson is the author of four books and many articles dealing with various aspects of information technology and its relationships to economic, political, and social issues. Ferguson is a life member of the Council on Foreign Relations, a director of the French-American Foundation, and supports several nonprofit organizations

Synopsis of the book:

The documentary, being split into five parts, starts by observing the deregulation and privatization of the banks of Iceland in 2000. After the bankruptcy of Lehman Brothers and the collapse of AIG, there was a worldwide stagnation.

After being deregulated for a long period of time, American financial industry was regulated during the time period of 1940 to 1980. By the time 1980s had ended, there was a savings and loan crisis which had resulted in costing the tax payers around $124 billion. In 1990s, Commodity Futures Modernization Act of 2000 refused efforts to regulate derivatives. In late 1990s, a small number of huge financial firms had merged. Investors had also suffered losses in March 2000 due to Internet Stock Bubble Burst. This led to investors facing a loss of $5 trillion. Five investment banks, namely Goldman Sachs, Morgan Stanley, Lehman Brothers, Merrill Lynch, and Bear Stearns, two financial multinationals and three insurance companies had dominated the industry. Loans were given which could not be paid back.The second part of the movie talks about the housing boom. In 2006, AAA-rated instruments flew from 2000 to 4000. CDOs were sold worth more than $3 billion. Low value CODs were sold as high-quality ones. Credit default swap was similar to an insurance policy. Subprime mortgages funded various CDOs. The amount of money loaned out by investment banks as compared to the assets owned by the bank touched exceptional levels.

The third part of the movie focuses on the crisis. CODs market had badly collapsed and investment banks had billions of dollars of loan to be repaid which was difficult. In November 2007, the great recession had begun. Companies started to collapse and all entities having AA or AAA ratings were on the verge of collapsing. Bank of America acquired Merrill Lynch. Worldwide financial system came to a standstill and led President Bush to signing Troubles Asset Relief Program. It wasn't much helpful though as worldwide stock markets constantly collapsed.

Despite the fact that economy all over the world was in shambles after the housing crisis in USA, the responsible executives of the investments banks and insurance companies had all their personal fortunes intact and in addition they also received supplementary bonuses from the money they got from TARP. Such actions were only made possible because the banking industry created an atmosphere which was to bribe all opinion leaders in a subtle and explicit manner subject to their requirement. They had their supporters in the government, regulators and even academia, such massive intrusion of the banking executives did help them a lot in covering up one of the largest scams in the history of mankind, wiping of trillions of dollars from the world' financial markets.

Unfortunately, despite the massive losses in the markets which not only wiped of equity but also cost millions of jobs worldwide, there are still no regulations in the system instead the regulations were further reduced in US markets, which appointments of Wall street lobbyists in Fed Reserve and Obama administration, while the European markets strengthen their regulator bodies and placed stringent regulation.

Key Learning:

The invention of derivatives and bundles of debt instruments that in some way left everyone (barring American homeowner / buyer and Chinese factory worker) a timeless winner was both perceived and encouraged by individuals and companies whose names are the ultimate icons in the world of finance. And I use the present tense, because as the film deftly displays, they are all still there, in the engine room and at the helm of the global financial machine.

Few escape blame, but Alan Greenspan, Larry Summers, Timothy Geithner, and so many others are identified by name. Many refused to be interviewed for the film, but many agreed and then sat in front of the camera crucifying themselves. Above all there were two areas of revealing compromise. Firstly the extent to which the AAA rating agencies are completely in bed with the companies they rate. Secondly that a cascade of the great "Ivy League" University Economics Professors are being paid millions by corporate America both to advise and to sit on their boards. According to the film, Harvard, Columbia, and other business schools have no regulatory system for monitoring these potential conflicts of interest.

The film sets out case after case of what it describes as gross criminality by known names, against whom no action has ever been taken. This is a completely 'must see' movie. But more, in this British Budget week, some may see it as a call to arms.

This is not just an American affair, this is global. In effect, the film demonstrates that no meaningful action has been taken to stop it happening all over again. Worse, that many of the agents of what went wrong, still have their hands on the major levers of global financial management.

1. *Derivatives are true weapons of mass destruction*
2. *You can get too big to fail*
3. *All you need to do is to bribe the right people in any way possible*
4. *Criminal justice system in USA is just as broken as a 3rd world country when targeting powerful*
5. *% growth in per capita income does not mean % growth in average citizens increase in income*

Application:

Pakistan 's central bank has proven to be a much better regulator than Fed Reserve that no such problems were witnessed by Pakistani banking sector, however during the same period there were different problems which surfaced in Pakistani market, owing primarily to political changes in the economy.

The operating environment of the financial sector experienced significant deterioration in 2007and 2008, due to a confluence of factors emanating from both the domestic and international economic and financial developments. While the domestic environment was characterized by weakening macroeconomic indicators and the uncertainty caused by the prolonged period of political transition, the global financial crisis and the commodity price hike had a feedback impact on the financial sector through the real sector of the economy. Pakistan, which remained largely unscathed from a direct impact of the crisis, has been more concerned with issues relating to monetary stability due to rising inflation since before the advent of the crisis. With a thriving banking sector, increasingly resilient to a wide variety of shocks, increasing but still relatively less correlation of domestic financial markets with global financial developments, a proactive and vigilant regulatory environment, and most importantly, no direct exposure to securitized instruments, risks to financial stability were largely contained and well managed as the crisis unfolded and impacted the financial sectors in advanced economies.

Grading Plan:

Areas	Marks
Author	1
Synopsis	2
Key learning	5
Application	2