

LESSONS FROM  
THE FINANCIAL  
CRISIS

# Contents

<b>Acknowledgments</b>	xv
<b>Editor's Note</b>	xvii
<b>Introduction</b>	xix
<b>PART I Overview of the Crisis</b>	<b>1</b>
<b>1 Leverage and Liberal Democracy</b>	<b>3</b>
<i>George Bragues</i>	
<b>2 A Property Economics Explanation of the Global Financial Crisis</b>	<b>9</b>
<i>Gunnar Heinsohn and Frank Decker</i>	
<b>3 Of Subprimes and Sundry Symptoms: The Political Economy of the Financial Crisis</b>	<b>17</b>
<i>Ashok Bardhan</i>	
<b>4 The Political Economy of the Financial Crisis of 2008</b>	<b>23</b>
<i>Roger D. Congleton</i>	
<b>5 The Global Financial Crisis of 2008: What Went Wrong?</b>	<b>31</b>
<i>Hershey H. Friedman and Linda Weiser Friedman</i>	
<b>6 The Roots of the Crisis and How to Bring It to a Close</b>	<b>37</b>
<i>James K. Galbraith</i>	
<b>7 Enron Rerun: The Credit Crisis in Three Easy Pieces</b>	<b>43</b>
<i>Jonathan C. Lipson</i>	
<b>8 The Global Crisis and Its Origins</b>	<b>51</b>
<i>Peter L. Swan</i>	

<b>9</b>	<b>Four Paradoxes of the 2008–2009 Economic and Financial Crisis</b>	<b>59</b>
	<i>John E. Marthinsen</i>	
<b>10</b>	<b>Understanding the Subprime Financial Crisis</b>	<b>69</b>
	<i>Steven L. Schwarcz</i>	
<b>PART II Causes and Consequences of the Financial Crisis</b>		<b>77</b>
<b>11</b>	<b>The Origins of the Financial Crisis</b>	<b>79</b>
	<i>Martin N. Baily, Robert E. Litan, and Matthew S. Johnson</i>	
<b>12</b>	<b>Ten Myths about Subprime Mortgages</b>	<b>87</b>
	<i>Yuliya Demyanyk</i>	
<b>13</b>	<b>The Financial Crisis: How Did We Get Here and Where Do We Go Next? New Evidence on How the Crisis Spread Among Financial Institutions</b>	<b>95</b>
	<i>James R. Barth, Tong Li, Lu Wenling, and Glenn H. Yago</i>	
<b>14</b>	<b>A Decade of Living Dangerously: The Causes and Consequences of the Mortgage, Financial, and Economic Crises</b>	<b>103</b>
	<i>Jon A. Garfinkel and Jarjisu Sa-Aadu</i>	
<b>15</b>	<b>Making Sense of the Subprime Crisis</b>	<b>109</b>
	<i>Kristopher S. Gerardi, Andreas Lehnert, Shane M. Sherlund, and Paul Willen</i>	
<b>16</b>	<b>Miraculous Financial Engineering or Legacy Assets?</b>	<b>119</b>
	<i>Ivo Pezzuto</i>	
<b>17</b>	<b>The Making and Ending of the Financial Crisis of 2007–2009</b>	<b>125</b>
	<i>Austin Murphy</i>	
<b>18</b>	<b>The Subprime Mortgage Problem: Causes and Likely Cure</b>	<b>133</b>
	<i>Ronald D. Utt</i>	
<b>19</b>	<b>Sequence of Asset Bubbles and the Global Financial Crisis</b>	<b>139</b>
	<i>Abol Jalilvand and A. G. (Tassos) Malliaris</i>	

<b>PART III</b>	<b>Borrowers</b>	<b>147</b>
<b>20</b>	<b>The Past, Present, and Future of Subprime Mortgages</b>	<b>149</b>
	<i>Shane M. Sherlund</i>	
<b>21</b>	<b>FHA Loans and Policy Responses to Credit Availability</b>	<b>155</b>
	<i>Dr. Marsha Courchane, Rajeev Darolia, and Dr. Peter Zorn</i>	
<b>22</b>	<b>The Single-Family Mortgage Industry in the Internet Era: Technology Developments and Market Structure</b>	<b>163</b>
	<i>Forrest Pafenberg</i>	
<b>23</b>	<b>Speed Kills? Mortgage Credit Boom and the Crisis</b>	<b>175</b>
	<i>Giovanni Dell’Ariccia, Deniz Igan, and Luc Laeven</i>	
<b>24</b>	<b>Subprime Mortgages: What We Have Learned From a New Class of Homeowners</b>	<b>181</b>
	<i>Todd J. Zywicki and Satya Thallam</i>	
<b>25</b>	<b>Rating Agencies: Facilitators of Predatory Lending in the Subprime Market</b>	<b>191</b>
	<i>David J. Reiss</i>	
<b>PART IV</b>	<b>The Process of Securitization</b>	<b>197</b>
<b>26</b>	<b>A Primer on the Role of Securitization in the Credit Market Crisis of 2007</b>	<b>199</b>
	<i>John D. Martin</i>	
<b>27</b>	<b>Incentives in the Originate-to-Distribute Model of Mortgage Production</b>	<b>209</b>
	<i>Robert W. Kolb</i>	
<b>28</b>	<b>Did Securitization Lead to Lax Screening? Evidence from Subprime Loans</b>	<b>217</b>
	<i>Benjamin J. Keys, Tanmoy Mukherjee, Amit Seru, and Vikrant Vig</i>	
<b>29</b>	<b>Tumbling Tower of Babel: Subprime Securitization and the Credit Crisis</b>	<b>225</b>
	<i>Bruce I. Jacobs</i>	

<b>30</b>	<b>The Incentives of Mortgage Servicers and Designing Loan Modifications to Address the Mortgage Crisis</b>	<b>231</b>
	<i>Larry Cordell, Karen Dynan, Andreas Lehnert, Nellie Liang, and Eileen Mauskopf</i>	
<b>31</b>	<b>The Contribution of Structured Finance to the Financial Crisis: An Introductory Overview</b>	<b>239</b>
	<i>Adrian A.R.J.M. van Rixtel and Sarai Criado</i>	
<b>32</b>	<b>Problematic Practices of Credit Rating Agencies: The Neglected Risks of Mortgage-Backed Securities</b>	<b>247</b>
	<i>Phil Hosp</i>	
<b>33</b>	<b>Did Asset Complexity Trigger Ratings Bias?</b>	<b>259</b>
	<i>Vasiliki Skreta and Laura Veldkamp</i>	
<b>34</b>	<b>The Pitfalls of Originate-to-Distribute in Bank Lending</b>	<b>267</b>
	<i>Antje Berndt and Anurag Gupta</i>	
	<b>PART V Risk Management and Mismanagement</b>	<b>275</b>
<b>35</b>	<b>Behavioral Basis of the Financial Crisis</b>	<b>277</b>
	<i>J. V. Rizzi</i>	
<b>36</b>	<b>Risk Management Failures During the Financial Crisis</b>	<b>283</b>
	<i>Dr. Michel Crouhy</i>	
<b>37</b>	<b>The Outsourcing of Financial Regulation to Risk Models</b>	<b>293</b>
	<i>Erik F. Gerding</i>	
<b>38</b>	<b>The Future of Risk Modeling</b>	<b>301</b>
	<i>Elizabeth Sheedy</i>	
<b>39</b>	<b>What Happened to Risk Management During the 2008–2009 Financial Crisis?</b>	<b>307</b>
	<i>Michael McAleer, Juan-Angel Jiménez-Martin, and Teodosio Pérez-Amaral</i>	
<b>40</b>	<b>Risk Management Lessons from the Global Financial Crisis for Derivative Exchanges</b>	<b>317</b>
	<i>Jayanth Varma</i>	

<b>PART VI</b>	<b>The Problem of Regulation</b>	<b>325</b>
<b>41</b>	<b>Regulation and Financial Stability in the Age of Turbulence</b>	<b>327</b>
	<i>David S. Bieri</i>	
<b>42</b>	<b>The Financial Crisis of 2007–2009: Missing Financial Regulation or Absentee Regulators?</b>	<b>337</b>
	<i>George G. Kaufman and A. G. Malliaris</i>	
<b>43</b>	<b>The Demise of the United Kingdom’s Northern Rock and Large U.S. Financial Institutions: Public Policy Lessons</b>	<b>345</b>
	<i>Robert A. Eisenbeis and George G. Kaufman</i>	
<b>44</b>	<b>Why Securities Regulation Failed to Prevent the CDO Meltdown</b>	<b>355</b>
	<i>Richard E. Mendales</i>	
<b>45</b>	<b>Curbing Optimism in Managerial Estimates Through Transparent Accounting: The Case of Securitizations</b>	<b>361</b>
	<i>Stephen Bryan, Steven Lilien, and Bharat Sarath</i>	
<b>46</b>	<b>Basel II Put on Trial: What Role in the Financial Crisis?</b>	<b>369</b>
	<i>Francesco Cannata and Mario Quagliariello</i>	
<b>47</b>	<b>Credit Rating Organizations, Their Role in the Current Calamity, and Future Prospects for Reform</b>	<b>377</b>
	<i>Thomas J. Fitzpatrick IV and Chris Sagers</i>	
<b>48</b>	<b>Global Regulation for Global Markets?</b>	<b>383</b>
	<i>Michael W. Taylor and Douglas W. Arner</i>	
<b>49</b>	<b>Financial Regulation, Behavioral Finance, and the Global Financial Crisis: In Search of a New Regulatory Model</b>	<b>391</b>
	<i>Emilios Avgouleas</i>	
<b>PART VII</b>	<b>Institutional Failures</b>	<b>401</b>
<b>50</b>	<b>Why Financial Conglomerates Are at the Center of the Financial Crisis</b>	<b>403</b>
	<i>Arthur E. Wilmarth</i>	

<b>51</b>	<b>Corporate Governance and the Financial Crisis: A Case Study from the S&amp;P 500</b>	<b>411</b>
	<i>Brian R. Cheffins</i>	
<b>52</b>	<b>Secondary-Management Conflicts</b>	<b>419</b>
	<i>Steven L. Schwarcz</i>	
<b>53</b>	<b>The Financial Crisis and the Systemic Failure of Academic Economics</b>	<b>427</b>
	<i>David Colander, Michael Goldberg, Armin Haas, Alan Kirman, Katarina Juselius, Brigitte Sloth, and Thomas Lux</i>	
<b>54</b>	<b>Fannie Mae and Freddie Mac: Privatizing Profit and Socializing Loss</b>	<b>437</b>
	<i>David Reiss</i>	
<b>55</b>	<b>Disclosure's Failure in the Subprime Mortgage Crisis</b>	<b>443</b>
	<i>Steven L. Schwarcz</i>	
<b>PART VIII The Federal Reserve, Monetary Policy, and the Financial Crisis</b>		<b>451</b>
<b>56</b>	<b>Federal Reserve Policy and the Housing Bubble</b>	<b>453</b>
	<i>Lawrence H. White</i>	
<b>57</b>	<b>The Greenspan and Bernanke Federal Reserve Roles in the Financial Crisis</b>	<b>461</b>
	<i>John Ryan</i>	
<b>58</b>	<b>The Risk Management Approach to Monetary Policy: Lessons from the Financial Crisis of 2007–2009</b>	<b>467</b>
	<i>Marc D. Hayford and A. G. Malliaris</i>	
<b>59</b>	<b>Reawakening the Inflationary Monster: U.S. Monetary Policy and the Federal Reserve</b>	<b>475</b>
	<i>Kevin Dowd and Martin Hutchinson</i>	
<b>60</b>	<b>The Transformation of the Federal Reserve System Balance Sheet and Its Implications</b>	<b>483</b>
	<i>Peter Stella</i>	

<b>PART IX Implications of the Crisis for Our Economic Systems</b>	<b>493</b>
<b>61 Systemic Risk and Markets</b>	<b>495</b>
<i>Steven L. Schwarcz</i>	
<b>62 The Transmission of Liquidity Shocks During the Crisis: Ongoing Research into the Transmission of Liquidity Shock Suggests the Emergence of a Range of New Channels During the Credit Crisis</b>	<b>501</b>
<i>Nathaniel Frank, Brenda González-Hermosillo, and Heiko Hesse</i>	
<b>63 Credit Contagion From Counterparty Risk</b>	<b>509</b>
<i>Philippe Jorion and Gaiyan Zhang</i>	
<b>PART X International Dimensions of the Financial Crisis</b>	<b>517</b>
<b>64 Only in America? When Housing Boom Turns to Bust</b>	<b>519</b>
<i>Luci Ellis</i>	
<b>65 The Equity Risk Premium Amid a Global Financial Crisis</b>	<b>525</b>
<i>John R. Graham and Campbell R. Harvey</i>	
<b>66 Australia's Experience in the Global Financial Crisis</b>	<b>537</b>
<i>Christine Brown and Kevin Davis</i>	
<b>67 Collapse of a Financial System: An Icelandic Saga</b>	<b>545</b>
<i>Tryggvi Thor Herbertsson</i>	
<b>68 Iceland's Banking Sector and the Political Economy of Crisis</b>	<b>551</b>
<i>James A. H. S. Hine and Ian Ashman</i>	
<b>69 The Subprime Crisis: Implications for Emerging Markets</b>	<b>559</b>
<i>William B. Gwinner and Anthony B. Sanders</i>	



<b>PART XI</b>	<b>Financial Solutions and Our Economic Future</b>	<b>569</b>
<b>70</b>	<b>The Long-Term Cost of the Financial Crisis</b>	<b>571</b>
	<i>Murillo Campello, John R. Graham, and Campbell R. Harvey</i>	
<b>71</b>	<b>Coping with the Financial Crisis: Illiquidity and the Role of Government Intervention</b>	<b>579</b>
	<i>Bastian Breitenfellner and Niklas Wagner</i>	
<b>72</b>	<b>Fiscal Policy for the Crisis</b>	<b>587</b>
	<i>Antonio Spilimbergo, Steven Symansky, Olivier Blanchard, and Carlo Cottarelli</i>	
<b>73</b>	<b>The Future of Securitization</b>	<b>595</b>
	<i>Steven L. Schwarcz</i>	
<b>74</b>	<b>Modification of Mortgages in Bankruptcy</b>	<b>601</b>
	<i>Adam J. Levitin</i>	
<b>75</b>	<b>The Shadow Bankruptcy System</b>	<b>609</b>
	<i>Jonathan C. Lipson</i>	
<b>76</b>	<b>Reregulating Fannie Mae and Freddie Mac</b>	<b>617</b>
	<i>Dwight M. Jaffee</i>	
<b>77</b>	<b>Would Greater Regulation of Hedge Funds Reduce Systemic Risk?</b>	<b>625</b>
	<i>Michael R. King and Philipp Maier</i>	
<b>78</b>	<b>Regulating Credit Default Swaps</b>	<b>633</b>
	<i>Houman B. Shadab</i>	
	<b>Index</b>	<b>641</b>