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What are the lessons for regulators from the 2008 global financial crisis?

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Isabella Zheng · 2 days ago

A friend of mine asked me about this question and I feel it might be suitable for a discussion here.

To answer this question, I thought about several points:
1. what caused the crisis?
2. is there any measures regulators can take at that time?
3. why did not the regulators try to avoid it?

For the first point, widely agreed ideas is the sub-prime mortgage crisis disappointed mortgage-backed securities. It leads to liquidity crisis later.

Second, Central Banks of many countries tried to control the liquidity crisis via fallback money. It still beyond controls. On Sep of 2008, some players under high leverage investment went bankrupt or taken by local government and triggered the crisis.

If we go back to two or three decades before, we can peel down the lure of sub-prime mortgage crisis. Credit spread and excessive borrowings push economic instantly but become a Trojan horse in long term.
For investors and brokers, under high return incentives, they believe securitization can reduce the risks of high-risk loan while later their expectations flawed.
Estate industry embroiled by securitization failure, sub-prime mortgage crisis fermented and surged around the world.

For the last question I do not have much ideas on it. I believe they want to do it but failed.

Beside this topic, I have another question: what role banks played in this crisis? If the bank can not ensure it can receive loans back with interests, why did they lent it out?

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Anonymous · 11 hours ago

I have a cynical interpretation of the 2008 crash. My answer to your question 1 is that wall street was trying to suck more money out of the population, but the population was broke. Credit card debt was maxed out and there were no more savings. So wall street, through the banks, started offering easy loans for houses to people with questionable ability to pay.

This gets those people paying off the loans for awhile and feeding capital into the banks who then give it to corporations for investment. When the loans go bad the banks can just repossess the houses, so they don't lose on the bad loans in the long run. The banks tried to hide the bad loans by packaging them with some good loans and selling them to investors.

The stock market crashed because wall street had pumped it up enough, so the big investors scooped off the money of the small investors, as they always do.

The reason the USA and Europe had no more capital is because it has all gone to Asia. Wall street will try one trick after another to get capital, but they cannot use the stimulus and QE that they used this time. So the answer to your question 2 is that the Fed has no more cards to play.

My analysis is probably flawed, which is why I need to take economics courses, and I would welcome a correction.

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Henry jacob ajoboru · 7 hours ago

This sounds like a conspiracy theory not an economic explanation...

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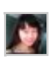 Isabella Zheng · 6 hours ago

I wrote a long passage but mistakenly fresh the page...
Basically I am saying that there are some people created bubbles the market can not cover.
When the bubble broke in a sudden, crisis began.

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+ Comment

wai chiu chan · 10 hours ago

There is no free market economy and the degree of government intervention depends on the state of the economy. The sub prime situation was due to over-spending of future income by consumers and encouraged by the irresponsible financial institutions. As long as the future income or production is on capital goods which will generate additional productivity and income, this should not lead to the crash. The consumption of future resource which should be long to the next generation should not be promoted and continue. However, the over regulated economy can restrict the GDP growth and put the economy unproductive and even in recession.

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Isabella Zheng · 6 hours ago

I like your idea.

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Henry jacob ajoboru · 7 hours ago

Banks lend against the future cash flow of an individual or organisation not necessarily against the asset being purchased which is also called the collateral. Now due to the recession, when people lost heir jobs and cannot pay their loans, the banks have to repurchase the house...however the house can't be turned to liquid cash until someone buys the house. When people don't wantto buy beause of the recession,then the banks are stuck with houses on their balance sheets which cannot be converted to cash to pay those who had initially brought their savings to the banks and would need them tommorrow.

The government bailing the banks is actually bailing the depositors because if the banks go down,the people loose their savings

The Banks couldn't have planned from day one that people won't be able to pay...yes lending to people who did not have sufficient capacity to repay is risky and irresponsible, however I do not think the clear intent was to ensure they cannot pay. If it is, then they shouldn't be bailed out for any reason...

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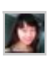
Isabella Zheng · 6 hours ago

very interesting idea. I like it.

However, I believe under smooth and prosperous environment, people tend to spend more as they believe they can cover the costs. This action accompany with loose censorship on credit blow finance bubbles. So we will have some unbelievable fancy years in advance while later suffered from the crush on advancing purchasing.

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Oluwatoyosi Lewis · 5 hours ago

One of the major lessons to be learnt by the regulators in light of the recent crisis is that conventional monetary policy tools do not always work. To the extent that the base rate (Fed Funds rate) was cut to 0.5%, this still did not significantly alter business and consumer confidence. What policymakers had failed to anticipate was the huge amount of debt that households had racked up and providing expansionary monetary policy (via lower interest rates) did not induce consumers to spend more,

The underlying problem of the recent crisis, which started in the housing market, seems to be rearing its head again. Asset bubbles are created when people are made to feel "rich". Providing guarantees for potential homeowners and leading them to believe they can afford mortgages in an era of low rates, will only lead to people struggling to keep up with repayments once rates rise (as they eventually will). Financial repression (low rates) is also not helping savers.

Policymakers need to be more innovative in applying tools that can aid the recovery. Deal with the root cause of societal problems (inequalities, etc) by providing the necessary social infrastructure. Propping up the housing market thinking the housing sector will always drive economic recovery is always going to lull consumers into a false sense of economic prosperity.

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