**Title:** Timeline of the Financial Crisis, According to All The Devils Are Here

**Subject:** The 2008 Financial Crisis

**Instructional Component Type:** Timeline

**Detailed Description:** This is an account of the major events that led up to the 2008 financial meltdown, the causes of which are extremely complex and multi-faceted. Our story begins in the late 1970’s, just as the baby boom generation was growing up and beginning to want homes of their own. Unless you were extremely wealthy to the point where you could pay the total cost of your new home with the cash in your bank account, you would need to borrow money in the form of a mortgage, which is a loan that can be paid back over the course of 30 years or so. However, because of the unprecedented size of the baby boom generation- “there were 76 million births between 1949 and 1964- many economists worried that there wouldn’t be enough capital to fund all their mortgages” (5). That all changed with the invention of something called the **‘mortgage-backed security’** in the late 1970’s by Lewis Ranieri of the Salomon Brothers firm in New York. The mortgage-backed security, according to All The Devils Are Here, “allowed Wall Street to scoop up loans made to people who were buying homes, bundle them together by the thousands, and then resell the bundle, in bits and pieces, to investors” (4). Basically, the effect that this had was to make a very risky investment (30-year mortgages) seem less risky to investors. Through a process known as **“securitization”**, Wall Street firms became able to essentially convert a very risky **mortgage** into a much less risky **bond.** The **mortgage bond** that resulted could then be split up into pieces and sold to investors, piece-by-piece. If that sounds confusing, that’s because it is!

**And So It Begins…**

-Late 1970’s- Lewis Ranieri of Salomon Brothers helps create the **mortgage-backed security,** adapting an idea that had actually been pioneered by U.S. government-sponsored organizations **Fannie Mae** and **Freddie Mac** (more on them later).

**-**1981-By this time, an estimated $350 billion had already been invested into these **mortgage-backed securities.**

-1983- By this time, the vast majority of the money invested in **mortgage-backed securities** was invested in the **government-sponsored enterprises (“GSE’s”)** known as **Fannie Mae** and **Freddie Mac** as opposed to privately-owned Wall Street firms. Fannie Mae and Freddie Mac were essentially private companies themselves, but they had the advantage of being backed (implicitly) by the full faith and credit of the U.S. government (or at least everyone thought so at the time…)

-1984-1986- Two crucial pieces of legislation passed under the Reagan administration (“SMMEA” and “REMIC”) led to an explosion in the market for **mortgage-backed securities** by essentially giving Wall Street firms a chance to get in on the profits being reaped by Fannie Mae and Freddie Mac.

-1988- Guardian Savings & Loan, run by Russell and Rebecca Jedinak, sold the first **subprime mortgage-backed securities**. A “subprime mortgage” refers to a mortgage loan given to somebody who doesn’t qualify for a mortgage from Fannie Mae or Freddie Mac because of a poor credit score, and they typically involve higher fees and interest rates than other mortgages. “Over the next three years, the Jedinaks sold a total of $2.7 billion in securities backed by mortgages made to less-than-creditworthy borrowers” (30).

-1989- By this time, private mortgage companies had seized about 20% of the market from the local banks and savings & loan firms which had traditionally lent people the money to buy homes. By 1993, they would control more than half of that market.

-1992- By this time Countrywide Financial, led by an aggressive CEO named Angelo Mozilo, has become the nation’s largest originator of single-family home mortgages. Mozilo, “believed strongly in the importance of underwriting standards- that is, in making loans to people who had the means to pay them back” (21).

-1994- A 100-year-old bank (JPMorgan) produces a major innovation by creating the first **Credit Default Swap** (**CDS)**- essentially, a CDS is, “an insurance policy against the possibility of default” (60). “Default” refers to occasions when someone is unable to continue paying their mortgage. This allowed banks like JPMorgan to transfer the risk of default onto a 3rd party, thereby reducing amount of the money that the bank had to keep in reserve.

-1996- The Federal Reserve officially agrees that credit default swaps (CDS’s) justified reductions in the amount of money banks were keeping in reserve.

-1997-98- In direct contradiction to their CEO’s belief in underwriting standards, Countrywide Financial enters the subprime mortgage market, which was already booming by this time.

-2001- By this time, 50% of all mortgage loans guaranteed by the GSE’s Fannie Mae and Freddie Mac were made to low- or middle-income Americans. In order to meet this goal, the GSEs lowered their underwriting standards, “just as the subprime industry had done” (49).

-2007- Freddie Mac announced that it will no longer buy risky subprime mortgages. Countrywide Financial was forced to borrow $11.5 billion, and saw its credit rating downgraded to BBB+ (“the bottom rung of what was so-called investment grade” [9]). New Century Financial and American Home Mortgage Investment Corporations- two of the leading subprime mortgage lenders- are forced to file for bankruptcy.

-2008- The U.S. Treasury seized control of the GSE’s Fannie Mae and Freddie Mac, and were essentially forced to pay out $200 billion in cash to help the two organizations recover from mortgage default losses. Several of the nation’s largest financial institutions were on the verge of collapse, and in the coming weeks the government was forced to spend additional billions bailing out firms such as AIG and Lehman Brothers. President Bush signed the official bailout plan into law.

-2010- President Obama signed into law the Wall Street Reform and Consumer Protection Act, “unquestionably, the biggest change in the regulation of the financial industry since the aftermath of the Great Depression… the bill creates a process to liquidate failing companies, so that there is a reasonable alternative to bailouts” (358). President Obama pronounced that, “the American people will never again be asked to foot the bill for Wall Street’s mistakes”. Only time will tell…

**-Keywords:** Subprime Lending, Mortgage-Backed Securities, Fannie Mae and Freddie Mac, Wall Street Broker Dealers, Credit Default Swaps, Financial Meltdown, Financial Crisis, Bailouts