

PRINCETON DIPLOMATIC INVITATIONAL 2026



2008
Financial Crisis

Chair: Grace Zhao
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FROM YOUR DIRECTOR-GENERAL

Dear Delegates,

Welcome to PDI 2026! I am so excited to have you join us for what promises to be an incredible conference. I'm Eric, and I'll be serving as your Director-General for the next four days. I can't wait to get to know all of you throughout the weekend and help make this experience as rewarding as possible.

A little about me: I'm a second-year student majoring in Public and International Affairs with a minor in Computer Science. I'm originally from Chişinău, Moldova but have also lived in Kyiv (Ukraine), Moscow (Russia), Ankara (Turkey), and Baku (Azerbaijan) throughout my life. On campus, I am also involved in PMUNC and PMUNT, am an international student leader at the Davis IC, and write for the Prince. If I'm not doing any of those things, I'm probably listening to, playing, or geeking out about heavy metal.

I'm thrilled to be working with an amazing team of Chairs and Crisis Directors to bring you exciting and thought-provoking crisis committees this year. I hope you come prepared to dive deep into past, present, and fictional issues, push your negotiation skills to the limit, and engage with the diverse perspectives that make conferences like PDI so special. Most importantly, I hope that you have fun and make the most of your time here.

Feel free to reach out to me anytime with any questions or thoughts you might have. I look forward to seeing you in committee!

Sincerely,

Eric Mohorea '28 (em4523@princeton.edu)



FROM YOUR CHAIR

Dear Delegates,

Welcome! My name is Grace, and I will be your chair for this committee. This is the fifth committee I've staffed at Princeton and have made countless wonderful memories, so I hope this committee will be just as enjoyable and memorable for you. Beyond sharpening your MUN skills, I also hope this experience helps you gain a stronger understanding of economics, knowledge that is not only useful in committee but also in everyday life, from managing personal finances to making sense of the news.

I'm a senior at Princeton majoring in Operations Research and Financial Engineering with a minor in Quantitative and Computational Biology. Over the years, I've pursued a wide range of interests. I have run a debate camp, written Science Olympiad exams, presented at a Slavic history conference, rowed in the ocean, and worked on multiple yearlong investigative data journalism projects. For a long time, I've wanted to run a financial crisis committee because I believe the crisis format is uniquely suited to capture the chaos of global economic collapse. Having worked in the financial industry, I see the legacy of 2008 everywhere. The 2008 crisis shattered long-standing financial assumptions, gave rise to entirely new lines of business, and left a generation of professionals whose caution now shapes decisions at the largest financial institutions.

This year's committee will dive into the causes, consequences, and policy responses surrounding the 2008 financial crisis, with delegates experiencing over 20 months of chaos (July 2007 to TBD) in the span of three days. We will examine the role of banks, regulators, and governments in trying to reverse years of systematic risk and see many of you needing to do everything you can to still have a job and stay out of jail. You will have the opportunity to shape both immediate responses and long-term reforms. While role-playing as some of the most powerful organizations and individuals, you will wield significant influence, and I plan to allow a high degree of creativity. I am excited to see what you come up with. I strongly suggest everyone read the background guide thoroughly. (Not to toot my own horn, but) It should provide more than enough context to participate actively, while the suggested readings can serve as helpful tools for shaping policy decisions.

I'm extremely excited for this committee, and I hope each of you has fun. I know the technical aspects may be new, but please don't hesitate to ask questions. You can always reach me at grace.zhao@princeton.edu (please include "PDI" in the subject line and sign off with your school/delegation). I can't wait to meet you all soon!

Sincerely,

Grace Zhao '26



COMMITTEE DESCRIPTION

A fast-paced committee that will see delegates start in July of 2007, a pivotal time for the future of the global economic landscape. With hindsight as your secret weapon, can you survive the crash and write a better recovery? You'll play the many interlocking gears of this economic machine. From the Federal Reserve to mortgage lenders, the US government to Wall Street titans. Amidst the chaos, scheming begins: which CEO gets thrown to the wolves, and can Congress stop bickering long enough to pass anything?

TOPIC: THE 2008 FINANCIAL CRISIS

"Recession" has become the go-to buzzword for every economic hiccup. But for those who lived through the 2008 Great Recession, the word still hits like a foreclosure notice. It was a global economic rollercoaster no one wanted to ride, but everyone got strapped in anyway. 15 years later, its legacy pops up in Dodd-Frank Act's regulating energy speculation to the rapid response during the 2023 banking crisis. Behind every crash is bad math, blind optimism, and one guy insisting, "Housing prices only go up."

Economics and finance, while useful, often rest more on luck, panic, and vibes than anyone wants to admit. No prior knowledge required, but please read the rest of this background guide. As long as you know a middle schooler with no job probably shouldn't buy a house on a maxed-out credit card, you're ready to reimagine the 2008 crisis. By the end, you'll appreciate the once-mythical phrase "too big to fail" and the disastrous consequences of building a house out of dominos.

TOPIC:

The 2008 Financial Crisis

INTRODUCTION

Welcome to the 2007-2008 Financial Crisis Committee. On the surface, this is an economics committee, but don't be fooled. At its heart, this is a political and personal drama where money, power, and reputation collide. Delegates are stepping into the shoes of real-world figures who defined the crisis: Wall Street executives, federal regulators, congressional leaders, and Cabinet officials. Their actions, or inaction, between 2007 and 2008 determined whether companies survived, markets collapsed, and millions of Americans kept or lost their entire livelihood. Now, in this simulation, you hold the pen that can rewrite history.

With a special focus on speed and alliances, delegates will draft directives to implement immediate actions (e.g., Federal Reserve cutting interest rates, Congress proposing emergency legislation, or a bank CEO approving a buyout). Behind the scenes, delegates can submit crisis notes, private communications to family, staff, allies, or even the media, to advance their agendas, build alliances, and scheme against rivals. The pace is fast, the stakes are high, and decisions carry consequences that ripple across the entire simulation.

The committee includes characters drawn from across the

financial and political landscape. Some of you represent the titans of Wall Street: Jimmy Cayne of Bear Stearns, Ken Lewis of Bank of America, Charles Prince of Citigroup, and Martin Sullivan of AIG. These are leaders of institutions whose very names became synonymous with the crisis, with some as the cause while others as the unfortunate casualties. Others will step into the shoes of regulators and policymakers like Federal Reserve Chairman Ben Bernanke, Treasury Secretary Henry Paulson, or SEC Chairman Christopher Cox, who attempted (with varying success) to calm the storm. Finally, members of Congress, from Nancy Pelosi to Ron Paul, embody the political divide over whether intervention was necessary or reckless.

Each perspective matters: a CEO may be fighting for survival, while a legislator worries about voters' anger, and a regulator struggles to keep the entire system afloat.

Delegate power:

As delegates, you have several key tools at your disposal. These mechanics may be familiar to most crisis veterans, but it will be helpful to clarify them here, especially the unique power of Joint Crisis Notes in this committee.

Directives: Short-term actions, passed by the full committee, that dictate policy responses or institutional decisions. These are binding and can change the course of events in real time. Directives are required for actions such as the arrest of a CEO, public-private

collaborations (e.g., Congress partnering with companies), or any major policy changes for public or private institutions.

Crisis Notes: Private or public communications that let you maneuver behind the scenes, cutting deals, requesting data, or undermining rivals. Think of these as levers for personal influence. If you're the CEO of a company, any company wide changes should be addressed to the Board of Directors with compelling arguments. And of course, you can always attempt bribery, backroom deals, or other schemes commonly seen in a crisis committee.

Joint Crisis Notes: Beyond normal joint crisis notes, where multiple delegates collaborate on a single action, this committee **introduces a special layer of institutional power**. Because this committee spans the entire economic ecosystem, certain institutions can act collectively with special authority.

- If all Federal Reserve members **unanimously** agree to adjust interest rates or issue a monetary policy decision, they may do so through a joint note. This will trigger immediate public reaction without requiring a full committee directive (unless otherwise specified).
- Similarly, if all Congressional delegates unanimously agree on legislation, they may pass it through a joint note. However, such actions are automatically public and will have real-time political consequences.

Additional Notes:

The crisis cannot be solved by one player alone. You will need to form coalitions: banks aligning with regulators, Congress working across party lines (or not), to craft solutions that hold. And keeping with the sprits of MUN, committee wide powers are much more powerful than real life. After all, in the real world, if the Fed and congress directly tell a company how to run it will as a major over-reach, but this can be an important tool for this committee.

While you should stay grounded in plausibility and should anticipate the first few crises updates to be directly from history, keep in mind, history is not set in stone. You may attempt interventions that did not occur in real life, whether that means nationalizing a bank, letting an institution fail, or proposing radical financial reforms. The committee will aim to reach early 2009 with the possibility of the last committee session set in 2010 to determine long term policies reform.

On Page 10, there is a guide on important concepts. These are more in depth than a typical definition, and you should check there before googling because these are written in the context of 2007-2008 crisis.

Your Challenge:

By July 2007, the system was wobbling but had not yet collapsed. You have the benefit of hindsight, knowing the full scale of the disaster that lies ahead as well as the effect of policies that were ultimately implemented. Will you act early and

aggressively, or will political infighting and denial delay your response, deepening the recession?

Above all, remember this committee is not about dry spreadsheets or perfect economic models. It's about power, perception, and persuasion. A bank CEO may have billions in assets but no allies. A Congress member may have no money but plenty of political sway. In this room, you will shape the fate of the global economy. Will you write a better ending, or preside over an even greater collapse? The choice is yours.

HISTORICAL BACKGROUND:

ROAD TO 2007

The 2007–2008 financial crisis was the product of decades of financial policy shifts, regulatory choices, and innovations in credit markets. Understanding these long-term developments is essential for grasping why the U.S. economy and the global financial system were so vulnerable by 2007.

1920s Crash and Early Regulation:

The 1929 stock market crash erased about \$40 billion in market value in two months and triggered the Great Depression, with unemployment reaching 25% by 1933¹. Thousands of banks failed as depositors withdrew savings en masse. In response, the U.S. created the core regulatory framework that governed much of the 20th century.

¹ (FDR Library & Museum 2016)

• Glass-Steagall Act (1933)²:

1. Separated commercial banks (deposits and loans) from investment banks (securities trading). This directly led big banks at the time such as JP Morgan to split part of its business into Morgan Stanley.

2. FDIC (1933): insured deposits up to a fixed amount through a pool of money, restoring trust in banks, especially for small rural banks.

• Securities & Exchange Commission (1934): regulated securities markets to prevent fraud and manipulation³.

Mid-20th Century Stability:

From the 1940s–1960s, U.S. finance was relatively stable. Real GDP grew about 4% annually⁴, and household wealth expanded, especially through homeownership. Federal programs supported long-term, fixed-rate mortgages.

• Fannie Mae (1938) and Freddie Mac (1970): bought mortgages from lenders, created mortgage-backed securities (MBS), and expanded liquidity in housing finance.⁵

• GI Bill (1944): Created VA home loan benefit that guaranteed low-interest mortgages and loans for returning veterans, fueling suburban growth. Between 1944–1952, nearly

² (Maues 2013)

³ (US Securities and Exchange Commission 2013)

⁴ (U.S. Bureau of Economic Analysis 2025)

⁵ (U.S. Federal Housing n.d.)

2.4 million home loans were made to veterans under the bill.⁶

- By 1970, the U.S. homeownership rate reached 62%, up from about 44% in 1940.⁷

Consumer finance also broadened. Credit cards emerged in the 1950s with Diners Club (1950) and BankAmericard (1958, later Visa). By the late 1960s, revolving credit was becoming a normalized part of middle-class consumption. Household debt as a share of disposable income rose from around 30% in 1950 to 58% by 1970.

At the macro level, the U.S. experienced sustained growth, but inflationary pressures in the 1970s challenged stability. The 1973 oil shock and stagflation raised borrowing costs, eroded real wages, and led policymakers and lenders to argue that New Deal-era restrictions constrained innovation in a globalized economy.

Deregulation & Innovation (1980s-90s):

The late 20th century saw a systematic rollback of financial restrictions:

- Depository Institutions Deregulation and Monetary Control Act (1980): allowed banks to compete on interest rates.⁸
- Gramm-Leach-Bliley Act (1999): Repealed Glass-Steagall's separation of commercial and investment banking. Enabled conglomerates like Citigroup to combine lending, trading, and insurance; Accelerated consolidation already underway in

⁶ (Centre for Public Impact 2019)

⁷ (U.S. Department of Housing and Urban Development 1994)

⁸ (Robinson 1980)

financial services; Criticized for worsening “too big to fail” by extending the banking safety net; Also credited with easing the crisis by allowing easier acquisitions (e.g., Bear Stearns, Merrill Lynch) and reorganizations (Goldman Sachs, Morgan Stanley); Added consumer privacy protections, though its overall legacy remains contested.⁹

During this period, new credit instruments expanded rapidly:

- Collateralized Debt Obligations (CDOs) and complex derivatives repackaged pools of mortgages into securities sold worldwide.

- The global notional value of OTC derivatives rose from \$72 trillion in 1998 to \$220 trillion in 2004.¹⁰

- By 2000, the U.S. mortgage market itself was worth over \$6 trillion.¹¹

Crucially, oversight did not keep pace. The SEC allowed banks to use internal risk models for leverage requirements, and rating agencies often gave risky products “AAA” ratings.

Early 2000s:

After the dot-com crash (2000) and 9/11, the Federal Reserve cut interest rates to 1% in 2003¹². Cheap borrowing spurred a surge in housing demand, and what looked like a self-sustaining cycle of rising home values and credit growth was in fact built on leverage and risk. By the early 2000s, U.S. finance had entered a period of aggressive expansion in credit markets and complex instruments:

⁹ (Mahon 2013)

¹⁰ (Drees, et al. 2001)

¹¹ (Arestis and Karakitsos 2009)

¹² (Board of Governors of the Federal Reserve System (US) 2025)

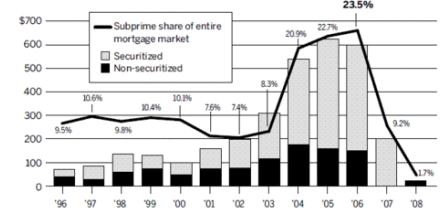
- Speculative Housing Market: Home prices rose nearly 90% nationwide between 1996 and 2006. Mortgage debt as a share of disposable income climbed from 61% in 1990 to 100% by 2007, while median home prices doubled from \$166,000 (2000) to \$313,000 (2006). Homes increasingly became speculative assets, not just places to live.¹³

- Subprime Lending: Mortgage credit expanded aggressively to less-qualified borrowers, with subprime loans growing from 8% of new mortgages in 2003 to about 20% in 2006. Many featured adjustable rates that reset higher after two years, creating built-in default risk.

Subprime Mortgage Originations

In 2006, \$600 billion of subprime loans were originated, most of which were securitized. That year, subprime lending accounted for 23.5% of all mortgage originations.

IN BILLIONS OF DOLLARS



NOTE: Percent securitized is defined as subprime securities issued divided by originations in a given year. In 2007, securities issued exceeded originations.
SOURCE: Inside Mortgage Finance

Figure 1 Numbers of new subprime mortgages from 1996 to 2008

- Securitization Boom: Banks bundled mortgages into mortgage-backed securities (MBS) and collateralized debt obligations (CDOs). Issuance of private-label MBS grew from \$130 billion in 2000 to over \$1 trillion annually by 2006. Risk appeared diversified but was actually concentrated.¹⁴

¹³ (Arestis and Karakitsos 2009)

¹⁴ (Federal Deposit Insurance Corporation 2018)

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- **Derivatives and Risk Transfer:** Credit default swaps (CDS) were marketed as insurance against defaults. But the market ballooned from \$900 billion in 2000 to over \$60 trillion by 2007, spreading risk across institutions in opaque ways.¹⁵

- **Leverage at Major Banks:** Firms like Lehman Brothers and Bear Stearns operated with leverage ratios of over 30:1. At that level, only a 3% drop in asset values could wipe out equity, making banks highly vulnerable once defaults rose.¹⁶

- **Regulatory Blind Spots:** The repeal of Glass-Steagall (1999) blurred commercial and investment banking, while over-the-counter derivatives markets remained largely unregulated.

- **Early Warnings:** Lenders like HSBC (a global bank with a large U.S. subprime book) issued profit warnings in late 2006 due to rising defaults. By the end of 2006, U.S. household debt reached about \$12.7 trillion, up nearly 10% year-over-year.¹⁷

By late 2006, cracks appeared: mortgage defaults ticked upward, housing prices slowed, and early stress emerged at lenders like Countrywide. Still, major U.S. banks and global investors, from Citigroup to European institutions, remained heavily exposed to mortgage-backed assets. The stage was set for systemic breakdown.

¹⁵ (Federal Deposit Insurance Corporation 2018)

¹⁶ (Board of Governors of the federal reserve system 2018)

¹⁷ (FEDERAL RESERVE BANK of NEW YORK RESEARCH AND STATISTICS GROUP 2025)

CURRENT SITUATION

Delegates will be starting on July 1st, 2007 after a series of domino that have all about guaranteed a global economic crisis. In Q1 of 2007, Housing Market's Home prices were already declining. The S&P/Case-Shiller Home Price Index showed its first year-over-year decline since 1991¹⁸. More than 25 subprime mortgage lenders had declared bankruptcy or exited the market by March 2007. New Century Financial, the second-largest subprime lender, filed for bankruptcy in April. Interest rates remain unchanged with The Federal Funds Rate standing at 5.25%, where it had been since mid-2006, putting pressure on borrowers with adjustable-rate mortgages.

By Q2, inventories of unsold homes rose sharply. In June 2007, over 4.2 million homes were for sale, an 8.8 months' supply, compared to 6 months considered normal¹⁹. Consumer Debt continue to rise with Household debt reaching nearly 130% of disposable income, a record high. Mortgage debt alone exceeded \$10 trillion, much of it tied to subprime and adjustable-rate loans. Bank leverage continue to be a problem. Major investment banks, including Lehman Brothers and Bear Stearns, were operating with leverage ratios near 30:1, meaning just a 3% fall in

¹⁸ (Federal Deposit Insurance Corporation 2018)

¹⁹ (U.S. Census Bureau 2025)

asset values could wipe out equity.

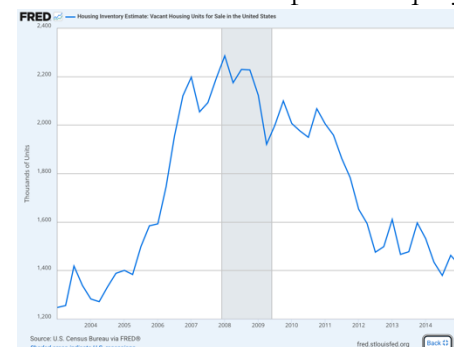


Figure 2 Housing inventory from 2004-2014

Now it is June 30th, 2007, the economy was evidently diverging from a slow correction into a broader unraveling. Housing markets were contracting sharply. Subprime loans, once a small segment, now posed widespread danger. Banks and mortgage issuers were visibly under strain, with stress at Bear Stearns and the bankruptcy of New Century acting as early red flags. Regulators and policymakers maintained steady interest rates, underestimating of the crisis's depth.

Consolidated Snapshot (as of July 1st, 2007)

Category	Highlight
Federal Reserve	Fed funds rate: ~5.25% ²⁰
Housing Market	Home prices down Q1: 6.7% quarterly, -14.1% YoY
Subprime Exposure	Loans worth ~\$1.3 trillion; 7.5 million subprime mortgages

²⁰ (Board of Governors of the Federal Reserve System (US) 2025)

Delinquencies	<u>ARM</u> subprime delinquency triple vs. 2005; Reached 20% for 2007
Household Debt	Reached ~128% of disposable income
Foreclosures	~1.3 million initiations in 2007 (+79% YOY)
Unemployment²¹	May: 4.4% June: 4.6% July: 4.7%

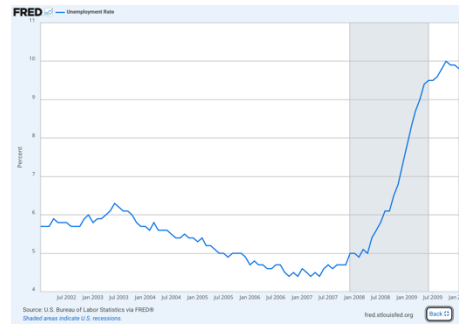


Figure 5 Unemployment Rate in the US from 2002-2010

KEY CONCEPTS

Recognizing this background guide and in your own research, you will come across many unfamiliar concepts, here it is quick rundown of important concept to help you succeed in this committee. This is meant to be more of an accessible definition in the context of 2008 than what might be considered most complete mathematical sound economic definition. Also, important to note, while economic are sometime considered a science, it is inherently political, so many concepts might have different interpretation. Delegates are encouraged to do future research on these, especially depending on what role they are, some might be more relevant than other.

Each definition includes a one sentence general description and its relevance to 2007-2008. These are separated into 3 categories. General economic concept, housing market/ mortgage crisis, and financial (institution) concepts. These are more technical but should be helpful for you to understand this background guide and any other research you decide to do.

General Economic Concepts

Loans – money borrowed that must be paid back. Repayment made up of two parts: Principal and interest. While one of the oldest financial tools, loans were spiraling out of hand by the mid-2000s, with consumer taking out a variety of loans from mortgage to credit card and banks increasingly dependent on risky mortgage lending to fuel profits.

Default – failure to pay back a loan. By late 2007, over 16% of subprime adjustable-rate mortgages were delinquent or in foreclosure, and each default not only harmed the lender but also destroyed confidence in mortgage-backed securities, freezing credit markets.

Debt – money owed by individuals, banks, or the government. Total U.S. household debt exceeded \$13 trillion in 2007, while financial institutions were leveraged at ratios as high as 30-to-1; when interest rates stayed high and asset prices fell, these debts became crushing liabilities.

Equity – The value of ownership in a company or asset, such as stock ownership or the portion of a home not owed to the bank.

GDP (Gross Domestic Product) – total value of goods/services produced in a country, often used to measure economic strength. From 2001 to mid-2007, U.S. GDP expanded at an average of about 3% per year, fueled by consumer spending and easy credit, but by June 2007 growth had slowed to near 1.5%. ²²The economy stagnated through 2008, and by

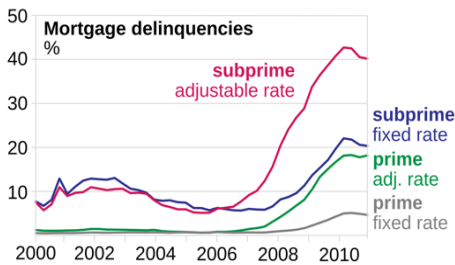


Figure 3 Rates of number of consumers that were behind on mortgage depending on type of mortgage.

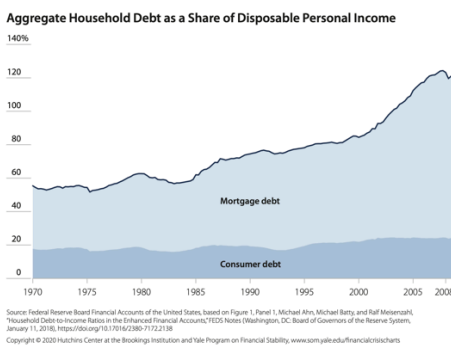


Figure 4 Aggregate household debt relative to disposable personal income from 1970-2008

²¹ (U.S. Bureau of Labor Statistics 2025)

²² (U.S. Bureau of Economic Analysis 2025)

2008 Financial Crisis

2009 GDP contracted sharply, marking the deepest downturn since the Great Depression.

Inflation – The general rise in prices over time, reducing the purchasing power of money. During periods of high inflation, consumers and businesses face higher costs, which can strain household budgets and corporate planning, and it can influence central bank policy decisions such as interest rate adjustments.

Recession – a period when the economy shrinks, often measured by two consecutive quarters of negative GDP growth. By late 2007, early signs of recession appeared as job growth slowed, consumer confidence fell, and housing prices dropped nationwide.

Stagflation – A combination of stagnant economic growth, high unemployment, and high inflation. Unlike typical recessions or periods of inflation, stagflation presents policymakers with the challenge of simultaneously addressing slow growth and rising prices, as seen in historical episodes like the 1970s oil crisis.

Liquidity – how easily assets can be turned into cash. For households, liquidity meant having enough savings to pay bills; for corporations and banks, it meant access to enough cash for short-term operations. In 2007, banks began running short on cash as mortgage-backed securities lost value, sparking panic, rising

interbank lending rates, and the first whispers of potential bank runs.

Bailout – government rescue of a failing company or bank that is considered central to the economy. In the 2008 crisis, this meant funneling billions of taxpayer dollars into major firms considered “too big to fail,” such as AIG, Citigroup, and Bank of America. While deeply controversial, these bailouts aimed to stabilize the financial system and prevent the collapse of credit markets.

Unemployment – A measure of people actively seeking work but unable to find it, making it one of the most direct indicators of economic distress for households. While a low level of unemployment (around 4–5%) is considered healthy for a dynamic economy, the 2008 crisis drove rates to 10%, compounding families’ inability to pay mortgages and deepening the housing collapse²³.

Housing Market Concepts

Mortgage – a loan used to buy a house. In the early 2000s, mortgages became widely available due to cheap credit and government-backed securitization, but by 2007, many borrowers were overextended, leaving both households and banks vulnerable when housing prices began to fall.

Subprime Mortgage – a loan given to someone with a higher risk of default. These loans exploded in the 2000s, often with little income verification and low teaser rates; by 2007, defaults on subprime

mortgages were surging, triggering massive losses on mortgage-backed securities and spreading risk throughout the financial system.²⁴

Credit – the ability of a borrower to obtain money or goods now and pay later, usually judged by a credit score that reflects their history of repayment. In the housing market, credit scores (along with income), determined whether borrowers qualified for prime or subprime mortgages, with lower scores often leading to subprime loans that carried higher interest rates and contributed heavily to the 2008 crisis.

Foreclosure – when a bank takes back a house because the borrower cannot pay. By 2007, foreclosure filings jumped 75% from the previous year, displacing families and flooding the market with distressed properties; many foreclosed homes were auctioned off at below-market prices, accelerating the drop in housing values and worsening the broader financial collapse.

Adjustable-Rate Mortgage (ARM) – a mortgage where the interest rate changes over time, unlike a fixed-rate mortgage that remains stable. ARMs were especially dangerous in the mid-2000s, as millions of borrowers faced steep payment increases when their “teaser rates” reset just as housing prices stalled and interest rates remained high from the 2006 peak.

Housing Bubble – when housing prices rise rapidly to levels much

²³ (U.S. Bureau of Labor Statistics 2025)

²⁴ (Arestis and Karakitsos 2009)

higher than their true economic value, often driven by speculation rather than genuine demand. Between 2000 and 2006, U.S. home prices rose over 80% nationwide, but when the bubble burst, values plummeted, it wiped out trillions in household wealth and setting off the chain reaction that fueled the 2008 crisis.

Financial Institution Concepts

Bank/Financial Institution – A company that handles money, loans, and investments, such as JPMorgan Chase or Citibank. These institutions take deposits, provide credit, and move capital through the economy.

Leverage – Using borrowed money to increase the potential return on an investment. For example, before 2008, many Wall Street firms operated at leverage ratios of 30:1, meaning just a 3% decline in asset value could wipe out their equity.

Securitization – The process of bundling multiple loans, such as mortgages, into a single financial product (like mortgage-backed securities) that can be sold to investors. This freed up banks to make more loans but spread risk across the global financial system.

Derivative – A financial contract whose value depends on the performance of an underlying asset, index, or loan. Derivatives can hedge risk or allow speculation; by 2008, the global derivatives market was estimated at \$600 trillion notional value.

Collateralized Debt Obligation (CDO) – A type of complex derivative made from bundled loans (e.g. subprime mortgages). At its

peak in 2006–2007, CDO issuance reached about \$500 billion per year, creating massive exposure to mortgage defaults.

Credit Default Swap (CDS) – A contract that insures against loan or bond defaults. For a premium, the seller of a CDS takes on the risk of default. By 2007, CDS contracts outstanding were about \$60 trillion notional, many tied to mortgage-backed securities. Because CDS didn't appear on bank balance sheets, they amplified hidden exposure to the housing market.

Risk – The possibility of losing money or facing financial harm due to uncertain events. In 2008, this included credit risk (borrowers defaulting on mortgages), market risk (housing prices falling more than 30% nationally), liquidity risk (banks unable to access short-term funding), and counterparty risk (institutions like Lehman Brothers failing to pay obligations).

Liabilities – Financial obligations a company owes to others. While it is usually part of normal business operations, when they grow too large relative to assets or are funded with short-term borrowing, especially on risky investments, they become dangerous.

Bank Runs – When many depositors withdraw funds at once due to fear the bank will fail. No bank ever has every person's money as liquid cash, so sudden loss of confidence can collapse even a solvent bank, as happened with Washington Mutual in 2008.

Shadow Banking – Lending and credit activities outside traditional banks, such as hedge funds,

structured investment vehicles, and money market funds. They often are heavily involved in money movement without having to follow traditional banking regulation. By 2007, shadow banking held almost \$20 trillion in assets²⁵, comparable to traditional U.S. banking sector.

Too Big to Fail – The idea that some institution, financial and otherwise (e.g. airlines, energy, tech), are so large and interconnected that their failure would cause systemic collapse. Oftentimes an official designation of TBTF give an implicit guarantee by the government of its support in time of turmoil. In 2008, the U.S. government committed over \$700 billion (via TARP) to stabilize major banks and insurers like AIG due to fear of cascading collapse.

Stress Test – A stress test is a simulation used by regulators to measure whether banks have enough capital to withstand severe economic downturns, such as spikes in unemployment or large declines in housing prices. After the 2008 financial crisis, stress tests became mandatory under the Dodd-Frank Act, with the Federal Reserve requiring large banks to regularly prove their resilience under adverse scenarios. These requirements require higher capital buffers, improve risk management practices, and increase transparency.

GLIMPSE OF THE FUTURE²⁶

The Calm Before the Crisis

In June 2007, the Federal Reserve's Beige Book painted a

²⁵ (Noeth and Sengupta 2011)

²⁶ (Guillén 2015)

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picture of steady growth and modest optimism. Most districts reported expanding economic activity: consumer spending was up, luxury goods were selling, tourism was healthy, manufacturing was stable, and commercial real estate was gaining strength. Even in housing, the Fed's tone was moderate: residential markets were described as "soft" or "weak," but with little sense of imminent collapse. Loan demand was "steady," hiring was increasing, and wage pressures appeared under control²⁷. To policymakers, it looked like the U.S. economy was weathering high gas prices and isolated housing troubles. But with our crystal ball, we know that's not true. You are allowed and ENCOURAGED to look ahead to see what will happen after July of 2007. But none of these events are set in stone, so if your company is on track to go bankrupt, you can still change that. Here are some key events that might be helpful to research.

Short-term (July-Dec 2007)

- Bear Stearns Hedge Fund Collapse (July 2007)
- LIBOR-OIS Spread Blowout
- BNP Paribas Fund Freeze (Aug 2007)
- Northern Rock Bank Run (UK, Sep 2007)
- Fed Rate Cuts (starting Sep 2007)
- Officially Recession (Dec 2007)

Medium-term (2008 flashpoints)

- Bear Stearns Sale to JPMorgan (Mar 2008)

- From April to August, unemployment rose from 5 to 6%, the highest since 2003.
- Fannie Mae & Freddie Mac Conservatorship (Sep 2008)
- Lehman Brothers Bankruptcy (Sep 2008) AIG Bailout (Sep 2008)
- TARP Legislation (Oct 2008)
- Merrill Lynch takeover by Bank of America (Oct 2008)

Long-term / Forward-looking policy and global themes

- Iceland's Collapse & Recovery (2008–2011)
- Global Commodity Price Spike (2007–2008)
- Speculative Trading Limits
- Global Imbalances
- European Sovereign Debt Crisis (2010+): Greece, Ireland, Portugal

Post-crisis Regulation:

The Dodd-Frank Act of 2010 introduced new protections for consumers, tighter supervision of large financial institutions, and limits on excessive risk-taking, most notably through the Volcker Rule, which restricted banks from engaging in speculative trading with their own funds. Regulators also began conducting regular stress tests to ensure banks could withstand severe economic downturns, while international agreements like Basel III raised capital requirements, forcing institutions to hold larger reserves as a buffer against future crises.

QUESTIONS

- Beyond just economic numbers, how did the financial crisis affect the everyday lives of Americans?
- What role should government-sponsored enterprises such as Fannie Mae and Freddie Mac play in the housing market moving forward?
- Should bailouts fundamentally exist— from a free market perspective as well as a consumer protection perspective?
- When does government intervention (such as bailouts) cross the line from stabilizing markets to encouraging moral hazard?
- Who is ultimately responsible for the crisis, and where is the line between negligence and malicious intent?
- How did the lack of transparency in the shadow banking system worsen the crisis, and what reforms could address this?
- With terms like 'recession,' 'housing bubble,' and 'market crash' constantly in the news, how can we ensure the public is financially informed without creating unnecessary fear or panic?
- How might the nationalization of major financial institutions during the 2008 crisis have altered the course of economic recovery in the US, and what would be the potential benefits and challenges of such government ownership within the context of American capitalist principles and political realities?

²⁷ (Federal Reserve Bank 2007)

• Multiple bank run happened in 2023, but it was effectively mitigated. Looking ahead, what systemic risks—such as climate change, fintech innovations, or sovereign debt crises—could trigger the next global financial meltdown, and are current safeguards enough to prevent it?

FURTHER READING

Here are some more resources by category. There is also an estimate time to read/glance though each of them. Many of these will have much more information than you are expected to know. You're of course welcome to read the bibliography, but those tend to be more niche and less comprehensive.

Overview Video Crash Course:

<https://youtu.be/GPOv72Awo68?feature=shared> (12 min)

Overview Reading:

(10 min)

<https://www.federalreservehistory.org/essays/great-recession-and-its-aftermath>

(30 min, VERY comprehensive timeline, rec further research)

https://lauder.wharton.upenn.edu/wp-content/uploads/2015/06/Chronology_Economic_Financial_Crisis.pdf

Housing Specific:

(5 min)

<https://www.fhfa.gov/conservationship/history>

(15 min, international perspective, glance through)

<https://www.landecon.cam.ac.uk/sites/default/files/2023-03/wp08-09.pdf>

Emergency Economic Stabilization Act of 2008

(10 min)

<https://hotellaw.jmbm.com/files/2014/03/EESA-Section-by-Section-jmbm-.pdf>

(5 min)

<https://www.britannica.com/money/Emergency-Economic-Stabilization-Act-of-2008>

Lasting Legacy:

(5 min)

<https://www.imf.org/en/Blogs/Articles/2018/10/03/blog-lasting-g-effects-the-global-economic-recovery-10-years-after-the-crisis>

(30 min, focus on intro, section 2 and 3. Try to understand the graphs and notice the trend)

<https://www.federalreserve.gov/publications/files/financial-stability-report-201811.pdf>

Optional Reading:

(>30 min, excellent starting point for further research)

https://en.wikipedia.org/wiki/2008_financial_crisis

(>1 hour, go through green book, beige book, presentation, and statement. Highly recommend for delegates representing the Fed board)

<https://www.federalreserve.gov/monetarypolicy/fomchistorical2007.htm>

(>30 min, a technical retrospective by the fed chair)

<https://www.federalreserve.gov/newsevents/testimony/bernanke20100902a.htm>

(>30 min, chapter 1 of a book and it provide a very comprehensive background on everything leading up to 2008)
<https://www.fdic.gov/media/18636>

(>30 min, A chapter by chapter overview of the same book)
<https://www.fdic.gov/media/18626>

(>30 min, some good tables and information for research)
<https://fred.stlouisfed.org>

(>2 hour, an advance analysis on nonprime mortgage)
https://www.jchs.harvard.edu/sites/default/files/ubb10-1_0.pdf

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POSITIONS & PORTFOLIO POWERS

FINANCIAL INSTITUTION LEADERS

These delegates represent banks or mortgage companies that were the biggest players in the financial market. Many of them were heavily involved in subprime lending and mortgage-backed securities. They can directly impact the market, each other, investors, as well as lobby for favorable legislation. Good primary source to research could be financial statement (10k), public released statement, and legal documents from lawsuits about events of 2007-2009.

Bear Stearns Chairman/CEO: James Cayne – You became president & CEO in 1993 and chairman of the board in 2001. It is no secret your company is going through a tumultuous time, bailing out your own fund while facing a liquidity crisis. Your job will be focusing on both salvaging the company, placating investors, and deciding what the future will hold.

Citigroup Chairman/CEO: Charles Prince – You rose to the top of one of the largest global banks, with deep involvement in lending, trading, and securitization. Under your leadership, Citi took on risky mortgage-backed assets that left the company highly exposed. Your task is to restore investor confidence, manage growing losses, and chart a strategy that ensures survival in a collapsing market.

Bank of America CEO/Chairman: Ken Lewis – You oversee one of the nation's largest commercial banks, with significant exposure to mortgage lending. You've pursued aggressive acquisitions, including moves into the mortgage sector, that now weigh heavily on your balance sheet. Your role will be balancing expansion against mounting risks, deciding whether to double down or retreat in the face of turmoil.

Lehman Brothers CEO/ Chairman: Richard S. Fuld Jr. – You have been at the helm of Lehman for over a decade, transforming it into a powerhouse of mortgage-backed securities. But with massive leverage and crumbling asset values, your firm is on the brink. Your challenge will be navigating investor fears, stabilizing the company, and avoiding the fate of collapse that many expect.

Goldman Sachs Chairman/CEO: Lloyd Blankfein – You lead one of Wall Street's most influential investment banks, deeply embedded in trading, securitization, and global capital markets. Goldman Sachs made a historic transition from investment bank to a bank holding company in 2008, now it is up to you to decide if this will happen and if it even makes sense to do it.

JPMorgan Chase Chairman / CEO: Jamie Dimon – You run the largest U.S. bank by assets, combining commercial banking, investment banking, and consumer finance. Known for your risk discipline, you entered 2007 with a relatively stronger balance sheet than many others. You are not only fighting to protect your own institution but also emerging as a potential rescuer.

2008 Financial Crisis

American International Group (AIG) CEO: Martin Sullivan – You lead one of the world’s largest insurance firms, with enormous exposure through credit default swaps tied to failing mortgage assets. What once seemed like a profitable hedge has turned into a major liability. Your job will be convincing regulators, investors, and counterparties that AIG can survive, while finding ways to cover escalating obligations.

Countrywide Financial CEO/Chairman: Angelo Mozilo – You built Countrywide into the largest mortgage lender in America, pioneering aggressive subprime lending and securitization practices. Now, defaults are skyrocketing, and your firm sits at the center of the crisis. Your focus will be managing public scrutiny, shoring up the company’s finances, and ensuring its survival as the mortgage market implodes.

THE FEDERAL RESERVE

The Federal Reserve sets monetary policy, manages interest rates, and oversees systemic risk in the banking system. These delegates can influence liquidity and credit conditions. The federal reserve minutes and voting record are great resources to better understand each of these member’s positions.

Ben Bernanke – You became Chairman of the Federal Reserve in 2006, taking over from Alan Greenspan. A former Princeton professor and expert on the Great Depression, you now face the biggest financial test of your career as cracks spread through credit markets. Your role will be deciding how aggressively to intervene with rate cuts, liquidity support, or emergency lending. While every vote is equal within the Fed board, as the chair you need to keep your house in order.

Timothy Geithner – As President of the New York Federal Reserve, you sit at the center of Wall Street oversight. Your bank deals directly with major institutions like Bear Stearns, Citigroup, and Lehman, making you the Fed’s eyes and ears on systemic risk. Your challenge will be balancing backdoor support for troubled firms with broader financial stability, and deciding how far the Fed should go in extending its safety net to investment banks and hedge funds.

Janet Yellen – You serve as President and CEO of the Federal Reserve Bank of San Francisco, the largest regional Fed bank in terms of population and economic output. Known for your dovish stance and concern for unemployment as well as financial stability, you provide a counterweight to more hawkish voices inside the Fed. In this committee, your role will be shaping debate over whether to prioritize inflation control or financial system rescue as the crisis deepens. (Note: While historically she was rotated off in 2007, for the sake of this committee, this position will have normal voting power.)

OTHER REGULATORY POSITIONS

These leaders oversee housing finance, securities, and government fiscal policy. They can regulate or intervene in markets, approve programs, and influence legislation. A lot of these organization went through extensive changes during and after 2008, so please make sure to understand what their role was in 2007 and what changes could make your individual organization better.

CEO/President of Fannie Mae: Daniel Mudd – Fannie Mae is a government-sponsored enterprise (GSE) that expands mortgage lending by purchasing mortgages from lenders and securitizing them into mortgage-backed securities. Its role is to provide liquidity and stability to the U.S. housing finance system. From 2007–2008, Fannie Mae struggled with mounting losses on subprime mortgages, leading to its placement into federal conservatorship in September 2008.

CEO/President of Freddie Mac: Richard Syron – Freddie Mac is a government-sponsored enterprise that operates in the secondary mortgage market by purchasing mortgages, bundling them into securities, and selling them to investors. Like Fannie Mae, it works to maintain liquidity and affordability in housing finance. In 2007, Syron received nearly \$20 million in compensation, but by 2008 Freddie Mac was facing severe capital shortfalls from risky loans and was placed into government conservatorship alongside Fannie Mae.

Chair of the U.S. Federal Deposit Insurance Corporation (FDIC): Sheila Bair – The FDIC insures bank deposits, supervises certain financial institutions, and manages bank resolutions to maintain public confidence in the banking system. Appointed in 2006, Bair was known for her independent stance and emphasis on protecting depositors and taxpayers. She advocated for stronger foreclosure mitigation efforts and structured bank resolution processes, often pushing for accountability and limits on executive compensation in institutions receiving government support.

Treasury Secretary: Henry Paulson – As Treasury Secretary, Paulson advised the President on economic policy and coordinated the government’s response to financial instability. Previously CEO of Goldman Sachs, he was deeply familiar with global markets and had cultivated close ties with Chinese leaders, launching the U.S.–China Strategic Economic Dialogue in 2006. During 2007–2008, Paulson became a central figure in crisis management, designing the Emergency Economic Stabilization Act (EESA) and directing the Treasury’s interventions to shore up banks and markets.

SEC Chairman: Christopher Cox – The Securities and Exchange Commission (SEC) regulates securities markets, enforces disclosure rules, and protects investors from fraud. It oversees exchanges, broker-dealers, and credit-rating agencies. During the crisis, Cox was criticized for weak oversight of investment banks and derivatives markets, including the SEC’s failure to prevent excessive leverage at Lehman Brothers before its collapse.

US CONGRESS

These members influence legislation, oversight, and public policy responses to financial instability. Their positions may support or oppose government intervention as well as have varying opinion on specific policy. Make sure to read about your own character. A lot of the votes in 2007 were not cleanly along party lines, with people from both parties being for and against for a variety of reasons. To help you start your research, what each of these candidates feel about the Emergency Economic Stabilization Act of 2007 is provided but keep in mind EESA have yet been created in our timeline.

Ron Paul (R – Against EESA) – Paul rejected the EESA on principle, viewing it as an unconstitutional overreach that distorted free markets. He argued that the bailout rewarded reckless behavior and transferred the cost of failure from private firms to taxpayers.

Marcy Kaptur (D – Against EESA) – Kaptur opposed the EESA because she believed it prioritized rescuing Wall Street over protecting working-class families who were losing their homes. She felt the bill socialized losses for big banks while doing little to address the root causes of the foreclosure crisis.

2008 Financial Crisis

Mitch McConnell (R – For EESA) – McConnell supported the EESA reluctantly, framing it as a tough but necessary choice to avoid systemic collapse. He underscored the importance of protecting not just banks but the broader economy, including businesses and households.

Chris Dodd (D – For EESA) – Dodd backed the EESA because he saw it as essential to restoring liquidity and confidence in the financial system. At the same time, he pushed for stronger regulatory frameworks to prevent similar crises in the future evident by being an architect of the Dodd Frank Act.

Nancy Pelosi (D – For EESA) – Pelosi supported the EESA as a necessary, though imperfect, measure to stabilize markets and prevent deeper economic fallout.

Richard Shelby (R – Against EESA) – Chair of the Senate banking committee from since 2003. Notably, in 1999 he was the only Republican senator—and one of just eight senators overall—to vote against the Gramm–Leach–Bliley Act, which repealed key provisions of Glass–Steagall, reflecting his long-standing concern about financial deregulation and systemic risk.