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# Stability in World Financial Markets: Introductory Remarks

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# SYMPOSIUM

# STABILITY IN WORLD FINANCIAL MARKETS: INTRODUCTORY REMARKS*

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Fordham University School of Law sponsors a class on Derivatives and Risk Management, which I teach. In this class we synthesize mathematics, economics, and legal analysis to demonstrate the regulatory framework in which the derivatives market operates.

Recent headlines emphasize that the regulatory scheme is inseparable from the economic nature of these financial risk management tools. Participants in this market, members of corporate boards of directors, their counselors and advisors must begin a learning process on the nature of regulatory responsibility in this multi-trillion dollar industry. Today we are going to discuss how that regulatory scheme is affected by the economic realities of an ever-changing financial marketplace. Through enhanced understanding of market realities, regulators, academicians and market participants can work together to create a more stable world financial marketplace.

Our conference is especially timely. Our global economy is in an exciting period of change. We have a new currency, the Euro.[1] Perhaps the regulatory structures of the "new Europe" will determine the success of that currency. This is a time when the

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1. *See generally* Kathy Jones & Alan N. Rechtschaffen, *The Euro – Ready or Not: Trading Implications of the New Common Currency*, 22 FORDHAM INT'L. L.J. 786 (1999) (discussing the trading and financial implications of the establishment of the Euro, which became the common currency for eleven European nations as of January 1, 1999).

price of Yahoo! and the internet stocks has become as important as the price of the Thai Baht and the Brazilian Real.

Today we are going to talk about new market developments, new opportunities, and new market risks. The history of the law of derivatives and risk management is a story of headlines, scandals, and rogue traders. Recently, regulatory excitement surrounded a hedge fund called Long-Term Capital Management ("LTCM").[2] The story of LTCM and the steps taken by those involved to insure a well-functioning financial market will set the stage for tomorrow's regulation. Several of the guests at today's

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2. On September 23, 1998, with the encouragement of the Federal Reserve Bank of New York, fifteen major banks injected $3.625 billion into Long-Term Capital Management, L.P. [hereinafter LTCM], a private investment fund engaged in highly leveraged securities transactions based on advanced mathematical models, to prevent its collapse and potential default on an estimated $125 billion it had borrowed on $2.2 billion in capital. *See* Anita Raghavan & Mitchell Pacelle, *To the Rescue? A Hedge Fund Falters, so the Fed Persuades Big Banks to Ante Up; Firms to Lend $3.6 Billion as Long-Term Capital Loses on its Bond Bets*, WALL ST. J., Sep. 24, 1998 at A1 (reporting on an "extraordinary gathering" in which the Federal Reserve Bank of New York persuaded large banks to invest over $3.5 billion in LTCM in return for a 90% ownership stake, and to prevent a financial crisis should it unwind its positions); Steven Mufson, *What Went Wrong? Fund's Big Bettors Learned that Risk Trumps Math, History*, WASH. POST, Sep. 27, 1998, at H1 (corrected Sep. 29, 1998) (listing fourteen major banks and institutions which invested a total of $3.6 billion); Steven Syre, *Fleet, BankBoston in Syndicate Backing Troubled Hedge Fund*, BOSTON GLOBE, Sep. 26, 1998, at F1 (reporting that Fleet Financial Group had loaned $25 million to LTCM as part of the bail-out); Joseph Kahn & Peter Truell, *Troubled Investment Fund's Bets Now Estimated at $1.25 Trillion*, N.Y. TIMES, Sep. 26, 1998, at A1 (citing financiers' estimates that LTCM had leveraged borrowings of $125 billion into $1.25 trillion in open trading positions). The LTCM crisis led to increased public and governmental scrutiny of hedge funds, including congressional hearings. *See, e.g., Hedge Fund Operations: Hearing Before House Comm. on Banking and Fin. Servs.*, 105th Cong. 1 (1998) (opening statement of Rep. Leach) (stating that a failure on the magnitude of LTCM's and the Federal Reserve Bank's intervention "raise profound public policy questions ...."). For comprehensive information on LTCM's background and near-collapse, see Michael Lewis, *How the Eggheads Cracked*; N.Y. TIMES, Jan. 24, 1999, § 6, at 24; Carol J. Loomis, *A House Built on Sand*, FORTUNE, Oct. 26, 1998, at 110; Michael Siconolfi, Anita Raghavan & Mitchell Pacelle, *All Bets are Off: How the Salesmanship and Brainpower Failed at Long-Term Capital*; WALL ST. J., Nov. 16, 1998, at A1.

symposium participated in a direct and meaningful way in the story of LTCM. Today we will discuss, among other topics, what events like the near-collapse of LTCM may mean for long-term regulation.

New regulatory schemes will have broad effects on our world financial markets. Recently, the heads of major banks and market participants met in New York to discuss self-regulatory initiatives for the derivatives market place.[3] This reaction to the recent market headlines reminds me of something Thomas Paine said: "[P]anics, in some cases have their uses; they produce as much good as hurt. Their duration is always short; the mind soon grows through them and acquires a firmer habit than before."[4]

We are here to discuss new solutions. Hints as to the future of market regulatory momentum may be revealed in today's proceedings. The participants at the Fordham Derivatives and Risk Management Symposium will help guide market participants, readers, regulators, directors and officers in their participation in the global economy.

Our economy is strong. The stock market in America may get stronger, with increasing technological innovations and low interest rates. The economy may be on the verge of the greatest revolution since the turn of the last century by virtue of the speed of information flow, the miniaturization of goods, and the globalization of the world economy. Today's symposium will give us insight into the past, and foresight into the future of our global markets and the world economies.

3. This meeting resulted in the formation of the Counterparty Risk Management Policy Group [hereinafter CRMPG], which issued a report in June 1999 on counterparty credit and market risk management. CRMPG, IMPROVING COUNTERPARTY RISK MANAGEMENT PRACTICES (1999) (on file with the *Fordham Finance, Securities, and Tax Law Forum*).

4. THOMAS PAINE, *The American Crisis No. 1*, *in* COMMON SENSE, THE RIGHTS OF MAN, AND OTHER ESSENTIAL WRITINGS OF THOMAS PAINE 75, 76 (Meridian 1984) (1776).