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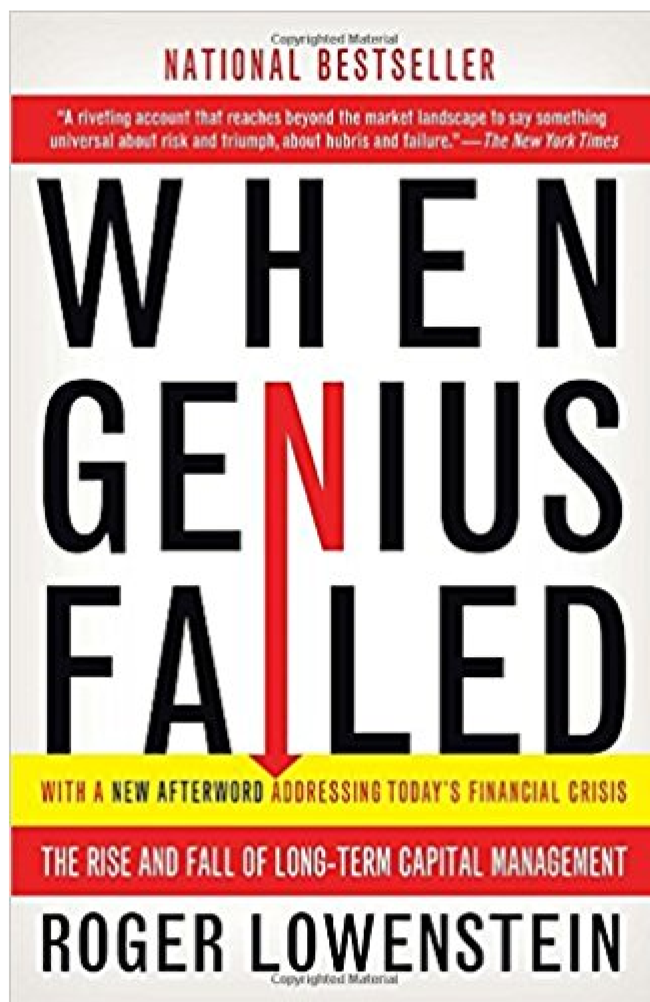
When Genius Failed: The Rise And Fall Of Long-Term Capital Management



Synopsis

With a new Afterword addressing todayâ ™s financial crisisA BUSINESS WEEK BEST BOOK OF THE YEARIn this business classicâ ”now with a new Afterword in which the author draws parallels to the recent financial crisisâ ”Roger Lowenstein captures the gripping roller-coaster ride of Long-Term Capital Management. Drawing on confidential internal memos and interviews with dozens of key players, Lowenstein explains not just how the fund made and lost its money but also how the personalities of Long-Termâ ™s partners, the arrogance of their mathematical certainties, and the culture of Wall Street itself contributed to both their rise and their fall. When it was founded in 1993, Long-Term was hailed as the most impressive hedge fund in history. But after four years in which the firm dazzled Wall Street as a $100 billion moneymaking juggernaut, it suddenly suffered catastrophic losses that jeopardized not only the biggest banks on Wall Street but the stability of the financial system itself. The dramatic story of Long-Termâ ™s fall is now a chilling harbinger of the crisis that would strike all of Wall Street, from Lehman Brothers to AIG, a decade later. In his new Afterword, Lowenstein shows that LTCMâ ™s implosion should be seen not as a one-off drama but as a template for market meltdowns in an age of instabilityâ ”and as a wake-up call that Wall Street and government alike tragically ignored.

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Customer Reviews

On September 23, 1998, the boardroom of the New York Fed was a tense place. Around the table sat the heads of every major Wall Street bank, the chairman of the New York Stock Exchange, and representatives from numerous European banks, each of whom had been summoned to discuss a

highly unusual prospect: rescuing what had, until then, been the envy of them all, the extraordinarily successful bond-trading firm of Long-Term Capital Management. Roger Lowenstein's When Genius Failed is the gripping story of the Fed's unprecedented move, the incredible heights reached by LTCM, and the firm's eventual dramatic demise. Lowenstein, a financial journalist and author of Buffett: The Making of an American Capitalist, examines the personalities, academic experts, and professional relationships at LTCM and uncovers the layers of numbers behind its roller-coaster ride with the precision of a skilled surgeon. The fund's enigmatic founder, John Meriwether, spent almost 20 years at Salomon Brothers, where he formed its renowned Arbitrage Group by hiring academia's top financial economists. Though Meriwether left Salomon under a cloud of the SEC's wrath, he leapt into his next venture with ease and enticed most of his former Salomon hires--and eventually even David Mullins, the former vice chairman of the U.S. Federal Reserve--to join him in starting a hedge fund that would beat all hedge funds. LTCM began trading in 1994, after completing a road show that, despite the Ph.D.-touting partners' lack of social skills and their disdainful condescension of potential investors who couldn't rise to their intellectual level, netted a whopping $1.25 billion. The fund would seek to earn a tiny spread on thousands of trades, "as if it were vacuuming nickels that others couldn't see," in the words of one of its Nobel laureate partners, Myron Scholes. And nickels it found. In its first two years, LTCM earned $1.6 billion, profits that exceeded 40 percent even after the partners' hefty cuts. By the spring of 1996, it was holding $140 billion in assets. But the end was soon in sight, and Lowenstein's detailed account of each successively worse month of 1998, culminating in a disastrous August and the partners' subsequent panicked moves, is riveting. The arbitrageur's world is a complicated one, and it might have served Lowenstein well to slow down and explain in greater detail the complex terms of the more exotic species of investment flora that cram the book's pages. However, much of the intrigue of the Long-Term story lies in its dizzying pace (not to mention the dizzying amounts of money won and lost in the fund's short lifespan). Lowenstein's smooth, conversational but equally urgent tone carries it along well. The book is a compelling read for those who've always wondered what lay behind the Fed's controversial involvement with the LTCM hedge-fund debacle. --S. Ketchum --This text refers to an out of print or unavailable edition of this title.

In late September 1998, the New York Federal Reserve Bank invited a number of major Wall Street investment banks to enter a consortium to fund the multibillion-dollar bailout of a troubled hedge fund. No sooner was the $3.6-billion plan announced than questions arose about why usually independent banks would band together to save a single privately held fund. The short answer is

that the banks feared that the fund's collapse could destabilize the entire stock market. The long answer, which Lowenstein (Buffett) provides in undigested detail, may panic those who shudder at the thought of bouncing a $200 check. Long-Term Capital Management opened for business in February 1994 with $1.25 billion in funds. Armed with the cachet of its founders' stellar credentials (Robert Merton and Myron Scholes, 1997 Nobel Prize laureates in economics, were among the partners), it quickly parlayed expertise at reading computer models of financial markets and seemingly limitless access to financing into stunning results. By the end of 1995, it had tripled its equity capital and total assets had grown to $102 billion. Lowenstein argues that this kind of success served to enhance the fund's golden legend and sent the partners' self-confidence off the charts. As he itemizes the complex mix of investments and heavy borrowing that made 1994-1997 profitable years, Lowenstein also charts the subtle drift toward riskier (and ultimately disastrous) ventures as the fund's traditional profit centers dried up. What should have been a gripping story, however, has been poorly handled by Lowenstein, who obscures his narrative with masses of data and overwritten prose. Agent, Melanie Jackson. Author tour. (Sept.) Copyright 2000 Reed Business Information, Inc. --This text refers to an out of print or unavailable edition of this title.

Roger LowensteinÃ¢Â Â™s book contains an extraordinary amount of detail. ThereÃ¢Â Â™s nothing wrong with that.The gist of the story is that no amount of financial modelling can overcome a Ã¢Â Âœblack swanÃ¢Â Â• event, even though the term Ã¢Â Âœblack swanÃ¢Â Â• was not a known term at the time of these events.Fast forward from 1998 to 2008 and the term Ã¢Â Âœblack swanÃ¢Â Â• has become a key piece of Ã¢Â Âœfinancial lexiconÃ¢Â Â• when considering what unforseen uncertainty might do to the value of financial assets and liabilities.With the benefit of hindsight, some of the geniuses at Long Term Capital Management might have considered financial modelling for a Ã¢Â Âœblack swanÃ¢Â Â• event.The story is also one for detailing the shortcoming and weakness of human character. For example:Ã¢Â Â¢ Hubris v humility;Ã¢Â Â¢ Arrogance v meeknessÃ¢Â Â¢ Over confidence v modesty;Ã¢Â Â¢ Pride v humility;Ã¢Â Â¢ Condescension v respect;Ã¢Â Â¢ Disdain v respect;Ã¢Â Â¢ Contempt v admirationand so it goes on.A reader is somewhat reminded by the verse Ã¢Â Âœas you shall sow, then so shall you reapÃ¢Â Â•. Such an apt phrase seemingly applies throughout the book, but the one stand out is when management decides to fully redeem the capital of the outside investors, with a view to increasing managementÃ¢Â Â™s share of the pie, only to find that the geniuses at Long-Term Capital Management had failed to realise that by shafting these investors, they had (in the end) shafted themselves.

When Genius Failed was a great read. Lowenstein did a terrific job of introducing the reader to the quirky personalities at Long Term Capital and their interactions with Wall Street, European and Asian investment banks and the Fed. The real genius of the book was that Lowenstein nailed WHY genius failed. The same lessons the professors and traders at Long Term Capital failed to learn are the ones that all traders need to know. Trading in the financial markets is art as well as science. Knowing what quantitative models can and cannot do, and knowing when a modelÃ¢Â Â™s underlying assumptions are violated are key to successful trading. And finally, having the humility to accept that no matter how smart you are (or think you are) the financial markets can and will periodically make you look like an idiot.

Although this novel was at times quite dense, it provided very fascinating insights into the world of Wall Street. It was not just a world of numbers, but rather competing unchecked egos, high-stakes, and a rejection of the potential for defeat. If you are not familiar with finance, this book can drag a bit. However, it does teach you a lot (despite its haughty tone and vocabulary). What is important here is how there are people behind the numbers-- and too often that is a fact overlooked by investors and Wall Street alike.

The book has relevant lessons - even some 20 years later. Covering the LTCM crash after the collapse of the Russian debt markets, the book really is a superb look at the risks and idiocy of pure formulaic finance and the danger of excessive leverage in light of both hubris and greed. The storyline of the book - with the rise and fall of LTCM is a decent read, and the book would likely rate 4 stars standing alone on the bulk. It is the "6 star" epilogue that brings up the grade. Lowenstein summarizes the lessons learned exceptionally well, and does so in a rather fair and unbiased way. The fact that this type of failure appears to recur with frightening regularity indicates that we don’t learn the lessons very well - and greed and hubris will generally rule the day - or at least The Street. A great book - even if you only read the epilogue.

Overall good book. Gives some inside info about the LTCM case that wasn’t widely known but at some parts the author over repeats the same things.Also he’s quite kind for the Nobel laureates and their models and also he doesnt talk extensively about themOverall though good and interesting book

I decided upon this book because although it has been almost fifteen years since the collapse of the hedge fund LTCM, the afterword was written in 2010, and I wanted to see what parallels there were between LTCM and the financial crisis of 2007-2008. Roger Loewensten describes how the extreme perils of derivative risk that brought down LTCM, were fundamentally the same risks that caused the financial crisis ten years later. He astutely notes that contrary to many observers, these events were not "the perfect storm," but rather largely poorly understood market forces. Although there is ample evidence of the greed of the LTCM partners, the decription of the formation and growth of the fund suggests it was the unmitigated hubris of the Nobel Laureates and other high IQ partners that contributed to the failure of this fund. This book is well written, with a focus on the participants rather than on the technical elements of hedging. As such, there is some confusion about how and why LTCM grew so leveraged, and why, as Loewenstein notes, their creditors were so beholden to them, and at such risk themselves as LTCM was failing. There are other sources for that information, and this book deserves the accolades it has received.

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