FROZEN ASSETS

Wall Street on the Tundra

Iceland’s de facto bankruptcy—its currency (the krona) is kaput, its debt is 850 percent of G.D.P., its people are hoarding food and cash and blowing up their new Range Rovers for the insurance—resulted from a stunning collective madness. What led a tiny fishing nation, population 300,000, to decide, around 2003, to re-invent itself as a global financial power? In Reykjavík, where men are men, and the women seem to have completely given up on them, the author follows the peculiarly Icelandic logic behind the meltdown.

BY MICHAEL LEWIS

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Just after October 6, 2008, when Iceland effectively went bust, I spoke to a man at the International Monetary Fund who had been flown in to Reykjavík to determine if money might responsibly be lent to such a spectacularly bankrupt nation. He’d never been to Iceland, knew nothing about the place, and said he needed a map to find it. He has spent his life dealing with famously distressed countries, usually in Africa, perpetually in one kind of financial trouble or another. Iceland was entirely new to his experience: a nation of extremely well-to-do (No. 1 in the United Nations’ 2008 Human Development Index), well-educated, historically rational human beings who had organized themselves to commit one of the single greatest acts of madness in financial history. “You have to understand,” he told me, “Iceland is no longer a country. It is a hedge fund.”
How did the economy get into this mess? Visit our archive “Charting the Road to Ruin.” Plus: A Q&A with Michael Lewis. Illustration by Brad Holland.

An entire nation without immediate experience or even distant memory of high finance had gazed upon the example of Wall Street and said, “We can do that.” For a brief moment it appeared that they could. In 2003, Iceland’s three biggest banks had assets of only a few billion dollars, about 100 percent of its gross domestic product. Over the next three and a half years they grew to over $140 billion and were so much greater than Iceland’s G.D.P. that it made no sense to calculate the percentage of it they accounted for. It was, as one economist put it to me, “the most rapid expansion of a banking system in the history of mankind.”

At the same time, in part because the banks were also lending Icelanders money to buy stocks and real estate, the value of Icelandic stocks and real estate went through the roof. From 2003 to 2007, while the U.S. stock market was doubling, the Icelandic stock market multiplied by nine times. Reykjavik real-estate prices tripled. By 2006 the average Icelandic family was three times as wealthy as it had been in 2003, and virtually all of this new wealth was one way or another tied to the new investment-banking industry. “Everyone was learning Black-Scholes” (the option-pricing model), says Ragnar Arnason, a professor of fishing economics at the University of Iceland, who watched students flee the economics of fishing for the economics of money. “The schools of engineering and math were offering courses on financial engineering. We had hundreds and hundreds of people studying finance.” This in a country the size of Kentucky, but with fewer citizens than greater Peoria, Illinois. Peoria, Illinois, doesn’t have global financial institutions, or a university devoting itself to training many hundreds of financiers, or its own currency. And yet the world was taking Iceland seriously. (March 2006 Bloomberg News headline: iceland’s billionaire tycoon “thor” braves u.s. with hedge fund.)

To read the complete story, pick up a copy of The Great Hangover: 21 Tales of the New Recession from the Pages of Vanity Fair (Harper Perennial), available online and at better booksellers now.

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