Lehman Brothers goes bankrupt, 15 September

Andrew Gowers, formerly of the FT and Lehman Brothers, on why the bank's luck ran out

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When Lehman Brothers was declared bankrupt my first thought was: ‘Oh shit, I can't believe this.’ I had signed my departure agreement on Friday 12 September at 5.20pm, so I was probably the last person who jumped off the ship before it sunk. Until the Sunday morning there was a feeling about the place that a deal would be done to save the bank. Obviously shareholders were going to be wiped out, but the US Treasury wouldn't let the whole thing go down with \$650bn of debt. But that is precisely what they did, and it could have been otherwise.

There was a political backlash gathering in the US Congress against endless bailouts for Wall Street. (Only the week before, Treasury Secretary Hank Paulson had rescued Freddie Mac and Fannie Mae.) Then there was the behaviour of Lehman's management itself, and Dick Fuld in particular. He had worn out his goodwill.

When Bear Stearns went down in mid-March that was the clearest sign that the world had changed. Lehman's share price fell by 48 per cent on that morning. A lot of people were dumbstruck: all you could see were all the traders transfixed by the screens. A terrible quiet descended on the place.

Lehman Brothers had a huge lump of toxic commercial real estate assets whose value was deteriorating, and these accounted for a disproportionate amount of burden on its balance sheet. The beginning to any solution would have involved tackling that, but they got to it too late - by the time they started to sell the prices were in a downward spiral.

Back in 2003, Warren Buffett talked about derivatives being financial weapons of mass destruction. He turned out to be right, but in the meantime lots of people made a hell of a lot of money out of them. In a way it was a confidence trick, that banks were allowed to lend vast amounts against puny amounts of capital - because of devices like securitisation, because of derivatives that were constructed out of mortgage securities. It was all right while house prices were rising: when prices fell and repossessions rose it went into reverse, and the market took fright at the capital position of the whole banking industry.

People say we shouldn't shed too many tears for bankers, but a lot of people suffered. The basic salary of even the very top people at the banks wasn't that great, but people were paid a gigantic proportion of their total compensation in restricted shares. You thought you had all this money in shares and you borrowed against them to finance your expensive lifestyle, and it's suddenly exposed as an illusion.

The government is able to get away with the idea that this is a disease made in the US that we've accidentally caught. But the British system created incentives for excess all of its own. Monetary policy was excessively loose, the authorities had a laissez-faire approach to asset bubbles, and they had a belief that they couldn't do anything about them. Banks are useful whipping boys.

It will never be the same as it's been in the past 10 years. It will be a very long and deep recession. One of the few pieces of good news on the horizon is Obama. His economic team is stellar, and he's showing real leadership even before he's taken office.