'The Big Short' Explained

What Is *The Big Short?*

The Big Short is a 2015 Oscar-winning film adaptation of author Michael Lewis's best-selling book of the same name. The movie, directed by Adam McKay, focuses on the lives of several American financial professionals who predicted and profited from the build-up and subsequent collapse of the housing bubble in 2007 and 2008.

Published in 2010, *The Big Short*: *Inside the Doomsday Machine* was a loose sequel to Lewis' best-selling *Liar's Poker*, a chronicle of his work experiences at Solomon Brothers in the 1980s. Both non-fiction works offer a deep dive into the lives, workplaces, and psychology of several Wall Street professionals and the financial world.

Key Takeaways

- *The Big Short* is a 2015 film adaptation of author Michael Lewis's best-selling book of the same name.
- Directed by Adam McKay, *The Big Short* chronicles the years leading up to the 2007-08 global economic crisis, focusing on several financial professionals (based on actual individuals) who predicted and profited from the collapse.
- *The Big Short* employs a novel stylistic approach: It frequently interrupts its narrative with cameo appearances by real-life authorities and celebrities, who explain complex financial instruments and practices with colloquial terms and examples.
- *The Big Short* won the Academy Award for Best Adapted Screenplay.
- Despite some criticism, *The Big Short* is generally acclaimed for its energetic, innovative, and even humorous depiction of Wall Street greed and the complicated events that led to The Great Recession.

Understanding *The Big Short*

The Big Short was not the first film adaptation of a successful non-fiction book covering the financial crisis. In 2011, HBO adapted Andrew Ross Sorkin's crisis tell-all *Too Big To Fail*, which also had a star-studded cast. That story centered more on the few weeks leading up to the collapse of Lehman Brothers and the government's decision to bail out the nation's largest banks and companies.

The Big Short, however, is a character-driven piece that focuses not just on the events leading up to the subprime mortgage meltdown, but also the conflicted feelings of several men (either real or based on real people) who foresaw the crisis well in advance. The film stars Christian Bale, Steve Carell, Ryan Gosling, and Brad Pitt.

One of those men is Michael Burry (Christian Bale), the manager of hedge fund Scion Capital. The year is 2005, and Burry begins to suspect the booming U.S. housing market is virtually an asset bubble inflated by high-risk loans. Burry creates a new sort of financial instrument, called a credit default swap, which would allow him to short the housing market—that is, sell positions, on the assumption that housing prices will drop.

When banks and creditors argue that the housing market is stable—and prices in fact do keep on surging—his clients grow angry and fearful as Burry continues his short plays. When they demand their money back, he places a moratorium on withdrawals from the fund, angering his clients even more.

Meanwhile, Deutsche Bank executive Jared Vennett (Ryan Gosling) inadvertently discovers Burry’s credit default swap creation, and—agreeing with Burry's analysis of the market—decides to start selling them. One of his clients is hedge fund manager Mark Baum (Steve Carrell). Baum recognizes that poorly structured, high-risk packages of loan securities known as collateralized debt obligations (CDOs) have received AAA ratings from credit rating agencies—implying a degree of safety they don't deserve—and are furthermore being repackaged and resold in highly questionable ways. It's financial institutions' appetite for these securities that is fueling much of real estate's rise—out of all proportion to the industry's fundamentals.

Like Burry and Vennett, Baum concludes that the housing bubble will ultimately pop, and may in fact lead to the collapse of the U.S. economy. He begins shorting the financial sector. (Baum was based on real-life hedge fund manager Steve Eisman. Vennett was based on Greg Lippmann, a former bond salesman at Deutsche Bank.)

A third plot strand follows two young investors—Charlie Geller (John Magaro) and Jamie Shipley (Finn Wittrock)—who discover a paper written by Vennett about credit default swaps. They seek the investment advice of retired banker Ben Rickert (Brad Pitt). Shipley and Geller make a series of successful bets against mortgage-backed securities and the housing market when it finally does start to collapse, making a fortune on their trades.

But Rickert lambasts them for profiting off the misery the mortgage meltdown has caused Middle America. The duo is left highly dejected about the moral hazard surrounding CDOs, having discovered that investment banks and credit rating agencies conspired to conceal the risks and prop up prices of the investments. They later try unsuccessfully to sue the rating agencies for their misleading rankings of mortgage-backed securities and mortgages. (Geller was based on Cornwell Capital founder Charlie Ledley, while Jamie Shipley was based on Cornwell partner Jamie Mai; Rickert was based on Ben Hockett, a former trader at Deutsche Bank.)

Burry, meanwhile, ends up producing nearly 500% returns for investors who stay with him through the duration of the housing market's collapse.

The Big Short FAQs

What Caused the 2008 Financial Crisis?

The financial crisis of 2007-2008 was years in the making, and due to a complex interweaving of causes. Its seeds were sown early in the decade, with cheap credit and lax lending standards fueled a housing bubble—an upward spiral in home prices as borrowers took advantage of low mortgage rates. Many of these loans were subprime—that is, the borrowers really couldn't afford them, putting the loans at high risk of default.

Lenders then sold those loans on to Wall Street investment banks, which packaged them into mortgage-backed securities and collateralized debt obligations. Rescinded regulations freed up banks and other institutions to borrow heavily to invest in these securities, which they then repackaged and sold to other investors.

By mid-decade, interest rates started to rise and homeownership reached a saturation point. Real estate prices started to drop, and people began to default on their mortgages. When the bubble burst in 2007, financial institutions were left holding trillions of dollars worth of near-worthless investments in subprime mortgages.

The interbank market that keeps money circulating around the globe froze—no one knew how widespread the losses were or who owed what, so they stopped lending completely.

By the summer of 2008, the carnage was spreading across the financial sector. Many venerable firms, like Bear Stearns and Lehman Brothers, went under. Lehman's collapse spooked the stock market, which went into free fall starting in late September.

3.8 million

Number of Americans who lost their homes due to foreclosure as a result of the 2007–08 collapse in the housing market, according to the Federal Reserve Bank of Cleveland.

The Bottom Line

The Big Short offers a highly engaging exploration into the years preceding the collapse of the housing market, which led to the Great Recession. In the end, it concludes, Wall Street greed sank the global economy for years.