

The financial effect of bernie madoffs ponzi scheme



Bernard L. Madoff, simply known as Bernie is an American allegedly the operator of what is known as the largest Ponzi scheme in history. Bernie before his capture, acted as the stock broker, investment advisor and non-executive chairman of the NASDAQ stock market (Cherry and Wong 11). It was not later than 2009 when Madoff pleaded guilty; he was guilty for turning his wealth management business into a massive Ponzi scheme. This scheme according to various sources defrauded thousands of investors billions of dollars (Cherry and Wong 16).

In 1960, Bernard Madoff founded one of the biggest firms in Wall Street. He was the chairman of his company “ Madoff Investment Securities LLC”, until his arrest was warranted on the December of 2008 (Forbes 21). Before his arrest, the Madoff Investment Securities emerged as one of the top market maker businesses on the Wall Street (Forbes 27). After his arrest, Madoff explained to his children as a confession that most of his asset management unit of his firm was none other but a big fraud.

The aim of this paper is to find out how Bernard L. Madoff managed to pull up the largest Ponzi scheme in history as well as the financial effects that this scheme had on the investors in the stock market. The Bernard Madoff Ponzi scheme left a lot of people financially wounded and as many people may think that this scheme only affect the Wall Street, research will prove otherwise. The Wall Street was just one of the victims of Madoff’s Ponzi scheme. Others include BSBC and Maxam Capital Management LLC. Just to name a few.

A Ponzi scheme is an investment where by fraud is involved. Usually when this scheme involves operations that pays returns to separate investors, not from the actual profit earned by the organization in question, but by profit from their own money or money paid by subsequent investors (Times 15). Due to its abnormally high but short term returns on investment, this scheme enables to entice new investors. Failure chances for this system are high mainly due to the fact that earning is usually less that the payment of the investors.

How it started and its Benefifers

According to Madoff, the Ponzi scheme began in early 1990s (All Sports New York 1). However, to the beliefs of the investigators or what they managed to scoop out of their investigations this scheme began earlier than that. Some say that the scheme began somewhere in the 1970s while others have different views. During the time huge amounts of money went missing from the client's accounts. The missing amounts included fabricated gains that were said to reach an estimate of \$65 billion dollars (credit card compare 13).

However, in order to pull out such a Ponzi is not an easy task. For one to be able to convince people to venture into a particular investment requires money and genius mind. Nevertheless, the main factor that made sure that Madoff was successful in his Ponzi scheme was his respect by other investors. He was also a well-established and esteemed financial expert with a reputation that was strengthened due to the reason that he was one of the founders of the renowned NASDAQ stock exchange and had a one term tenure as its chairman (How stuff works 2).

<https://assignbuster.com/the-financial-effect-of-bernie-madoffs-ponzi-scheme/>

He managed to earn the trust of his investors by his genius mind, since he ran his scheme concurrently; his was a legitimate business. He ensured that whenever his investors requested a withdrawal, Madoff Investment Company got their money to them promptly (How staff works 1). In addition to that, Madoff did not tempt his investors with unbelievable returns which were a problem of other schemers.

On the contrary, this scheme did not just benefit Madoff. Jeffrey Picower, appear to have benefited the most in the scheme as his estate settled the claims against it for a figure estimated to be around \$7.2 billion (Cherry and Wong 19). Another company that benefited more in the scheme is J. P. Morgan Chase & Co. their benefits were seen in terms of interest and fees charged which were to the tune of a billion dollars. Other investors too were included in the scheme and while some of them have decided to return the money that they gained from the scheme some have decided to deny their involvement in the Madoff Ponzi scheme.

Examples of the investors that have refused the charges include New York Mets owners Fred Wilpon and Saul Katz as well as other associated individuals and firms. These investors collectively received a collective amount of approximately \$300 million; however Wilpon and Katz have rejected their involvement (Forbes 4). Other investors are still unknown but with time it is assumed that most or all the parties involved in this so called 'one big lie' investment will be found with time.

His victims

The Bernard Madoff Ponzi scheme was declared as the largest Ponzi scheme in history. The so called largest fraud however has left big financial effects on the investors in the market. Most of these investors were directly linked to it while others were not. Thus in this section I am going to point out some of the victims that were affected by Madoff Ponzi scheme. To begin with, HSBC appeared to be among the largest victims of Bernard Madoff Ponzi scheme. The company became a victim of the fraud with a potential exposure of about \$1billion to the investment manager's collapsed venture (huffingpost 1).

In addition to that, HSBC's revelation resulted from loans it offered its institutional clients, mainly hedge funds that wanted to invest with Mr. Madoff (huffingpost 1). However, the \$1billion is said to be just a part of the cash provide in loans by customers who invested an approximate of \$500million of their own funds in Mr. Madoff's venture (huffingpost, 2011). To ease their lose, HSBC has been put first on the list whose money will be return, however this will only be to the success of the US authorities recovering any funds that went into Madoffs ventures.

On the contrary, Fairfield Greenwich Group was viewed as the greatest loser in this con of the century. The company lost an estimated amount of \$7. 3 billion in their Fairfield Sentry Ltd (businessinsider, 2011). Fairfield Sentry has a record of more than 15 years with an annual return of 4 to 6 percentage points above benchmark interest rates, this is a report put forward by a marketing document prepared by Zurich-based NPB New Private Bank Ltd (businessinsider, 2011). In a ten year period that ended in <https://assignbuster.com/the-financial-effect-of-bernie-madoffs-ponzi-scheme/>

2000, the company's interest rates ranged from 6.4% to 9.8%. This was due to the "split-strike conversion", where the investment manager is made to buy shares belonging to large companies in the US and then entering into options contracts to limit the risk (businessinsider 2).

In the wake of the Madoff Ponzi scheme, Fairfield Sentry Ltd Fixed Asset Management opened an account worth \$400 million with the Madoff investments. The news of their investment falling into fraud came to them as a shock since then they had been checking with lawyers.

Other potential victims to the Madoff Ponzi scheme are the giant French bank BNP Paribas, the Tokyo Based Nomura Holding Inc. and Neue Privat Bank in Zurich (WSJ 2). These two companies which raised lots of funds from investors and farmed out to hedge funds also suffered significant losses even though their loss was not compared to what Tremont Capital Management and Fairfield Greenwich Group, both of New York, had on the Madoff con of the century.

Another firm that suffered as victims of the fraud was Kingate Management Ltd who lost an approximate amount of \$2.5 billion while investing with Madoff (businessinsider 1). Thus while this seem to be a big loss Santander, which is known as the Eurozone's largest bank by market value lost an allegedly \$3.1 billion to the Madoff con (businessinsider 2). Santander had most there assets (2 billion euros) belonging to the institutional investors and international clients of its private-banking businesses (businessinsider 1).

The Madoff scam did not just affect corporations but also individuals who had invested heavily in the Ponzi scheme. According to Times a family in America was clearly wiped of their wealth overnight. On the 11 of December 2008, a wife received a call that they had been waiting for 5 years in the morning from the person handling their financial matters just to tell her that they were clearly wiped of their investment. To their knowledge, they did not know it but they had been involved in the grand scheme masterminded by Bernard Madoff (Times website 1). Their investment began after they had sold their home at the peak of the market; the wife had a divorce earlier so the settlement from the divorce too was included in the investment together with other petite amounts they had saved.

This however, is not the shocking news since the two lovers never really heard of the name Madoff. According to Times, their investment was carried on by a network organizer associated with Madoff. What attracted them was his 40 years fantastic achievement. Also the fact the wife's entire family was in the business for decades was enough to make them believe that their investment in Madoff's scam was a way forward.

However, that is not the only family that was affected by the Madoff scandal. Thyssen Family, although not much of a family but a corporation, was also at the mist of the saga. Businessinsider. com reported that the family had been fund of funds since 1989 (businessinsider, 2011). Their involvement in the Madoff Ponzi Scheme came as a guarantee that the investment was going to bring to them a huge return. Ira Roth's Family too was affected by the saga. The family had their \$1 million invested through Mr. Madoff's firm. Ira found

this to be a legitimate investment after finding out that his mother in law had been living on the investment's return (businessinsider 2).

The list of Madoff's victims goes on and on and thus making his story a very curious case to study. Most of the victims did not have a ware about of what they were doing. Despite the fact that Madoff himself was the owner of one of the top market makers companies on Wall Street was perhaps enough to blind people and make them think that all that he was offering them was a legitimate deal.

After effects

Bernard Madoff Ponzi scheme is seen as the biggest financial scam in history. However, this scam has left not just victims but also big after effects. Many corporations and individuals were left wondering which way forward they should take. Some of the individuals were completely wiped off their investment savings as well as ventures while others even though did not end up having nothing, need to return what they ventured in the scam.

The New York Mets owners Wilpon and Katz involvement in the Madoff's Ponzi is said to affect the Mets' record in various ways. The Wilpons are said to have invested heavily with Madoff, however they did not just invest their money but the Mets' money and money that did not belong to them (Forbes 4). The worst part is that the Wilpons invested money that belonged to the players as well as money they used to fund other projects and TV stations.

Despite the fact that, the Wilpons managed to get a lot of returns before the Madoff saga blew off, the saga has caused them now to put Mets on sale. At the beginning their allegations were that they were going to sell 20-25% of <https://assignbuster.com/the-financial-effect-of-bernie-madoffs-ponzi-scheme/>

the team and none of the SNY but in April 2010 Forbes valued the team together with the SNY at around \$825 million (Forbes 2). Their debt is still increasing and now both their team and the SNY are valued at around \$225 million. however much the Wilpons are trying to revive the Mets and prevent it from being sold, it is quite clear that their the teams after effects from the Madoff Ponzi Scheme has robbed them off the every other alternative but to sell both the SNY and the team.

However, the Madoff Ponzi scheme after effects was not just felt by individuals or corporations. This Ponzi scheme also had an effect on the stock prices as it forced scores of other hedge funds to dispose holdings and increase downward pressure on the stock prices (Forbes 2). These effects were seen after the arrest of the 70 year old investor who was widely considered to have a magic touch as an investor.

In addition to that, investors across New York who had clamored to be in Ascot because of their stability of double-digit returns proficiency and the findings of wealth multiplication have all been left with neither head nor tail of what was going on in the corporation (Forbes 3). However, while others were being affected financial wise, the exposure of the fraud on a substantial scale was a upsetting to individuals who put their trust on Madoff with their fortunes and also to non-profit organizations which include Yeshiva University. This university, counted much on Madoff's alleged clandestine trading system to assist operate its institutions (Forbes 2).

Justification on the Ponzi

Despite the fact that the Madoff Ponzi scheme left so many remnants, a question still remains can financial scam be justified? Many people who fall into financial scams are usually the wealthy type. However, seeming like that is not enough, it has been found that most of the big players of a financial scam are also the wealthy people. For instance the Mets proprietors spent a lot of cash in the scam and thus it was until the whole business failed that they all lost. Despite that this Ponzi left a lot of financial effects of people and corporations, it also left a lesson that will never be forgotten.

Madoff's Ponzi just like any other financial scam was not costly to only those who were directly involved but it also had a significant and a far reaching effect among societies nations and even worldwide (creditcardcompare.com. au 2). The Ponzi scheme was bigger than any other financial scandals which have included social security and mortgage mess. The people who have been following the story as it was being air on television and also in court are now asking themselves how much they can trust a corporation they want to invest in.

Bernard Madoff Scam cost around \$50 billion, and while it appeared to be the worst scam in history, it had its effects which were not just felt by the rich. However, its effects spanned to all nations in the worldwide. The rich together with the poor were all pulled by its magnet. The effect of this Ponzi scheme however has ensured that people will be more careful when it comes to investment. For instance, the two couples that sold all their properties just to invest on Madoff's ventures had not acquired the right information that

would have enabled them to actually know what kind of investment they were entering.

In a statement published on Times web site the couple stated that they did not know Madoff and thus their financial investment was being carried on by one of his network organizer. This is what smart investors will call lack of legitimate knowledge.

More than that, other corporations were caught into the saga since they wanted to increase their profits. Also the fact that Madoff owned a big corporation on Wall Street was enough to actually convince people that his dealings were not just profitable but also legitimate. This backfired for many of the investors. Thus it is very important to actually know the company in which you are investing on.

Many financial scams have come up before the Madoff Ponzi scheme but yet people are still being coned by these scam bugs. During the scam the effects are not realized. Even the person orchestrating the scam does not even think of what may happen at the end. It is until the end or after all hell has broken loose that many people come to realize that they were being coned. Thus this is what happened with the Madoff Ponzi scheme. It was not until people received phone calls that they realized that their investment ventures were just lies.

However, Forbes has it that, if Madoff had not faced the \$7 billion in redemption, the Ponzi scheme had not have been discovered (Forbes 2). This brings us to another lesson learned from this Ponzi 'greed'. Some believe that greed is virtuous, especially when referring to money. However how <https://assignbuster.com/the-financial-effect-of-bernie-madoffs-ponzi-scheme/>

much greed is good also becomes a question that people need to ask themselves. Madoff clearly knew that what he was doing was not right and thus probably he could have continued with it if he had kept it to the down low.

Nonetheless, it is still astonishing the rewards that Madoff managed to pull out of this false investment and thus smart people could have pulled out of it. This is because it is virtually impossible to actually accumulate hefty returns similar to what Madoff gained, and it should have served as a warning to the involved parties (Forbes 1). Instead of waiting until the end where you will be left shocked how such a financial fraud was possible it would have been better if people had actually got smart and start questioning the amount of wealth that was being generated by the Madoff invisible company.

Madoff may have conned many individuals, he may have left an investment scare on the financial market as many people are now left wondering where they should invest but in the long run people have to open their eyes.

Conclusion

In a nutshell it is quite clear that a financial investment can bring huge fortunes to someone. However, financial investments can also leave someone not knowing what has actually happened. Bernie Madoff Ponzi scheme is the latest financial scandal to have taken place and as if that is not enough it has also been labeled as the largest financial scam in history. This financial scam has left many people and corporations until now feeling

the effects of the Ponzi but the question still remains will this stop people from being financially conned?