

Goldman Sachs: “Financial Fraud!” What a Happy Noise. Revenge is Sweet.

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Schadenfreude. The pleasure derived from watching someone else suffer. It's human nature and it's what's what's driving the Goldman pile-on. SEC Enforcement director Robert Khuzami had barely uttered his statement on Friday, before the the yelps of joy arose from every corner of the country. “Fraud!” What a happy noise. Revenge is sweet. Suddenly the prospect of subpoenas, indictments, and long prison sentences didn't seem so remote. But don't get your hopes up. Goldman was picked for a reason, and that reason has nothing to do with its shady business transactions. It's politics.

Don't get me wrong; Goldman is guilty as hell. They slapped together a Kamikaze CDO that was designed to blow up, and then they schluffed it off on their clients without filling them in on the details. It's called “withholding material information”, and its no-no. It's like wrapping smelly fish in yesterday's paper and pawning it off as fresh-caught Blackmouth. You can't do that. According to former regulator William Black, “Goldman did not just withhold information, they told people, ‘Hey, the investment decisions are being made by experts who would only choose good quality stuff’, when in fact, the stuff that was put in was chosen because it was considered the most likely to suffer near-term downgrades.”

So Goldman was minting its own roadside bombs and getting input from notorious hedge fund short-seller, John Paulson, who planned to bet against the same CDO. But what's most shocking, is that Goldman was caught schtuping its own clients just to make a buck. That's going to haunt them for a very long time. Trust is important, even on Wall Street. Goldman's reputation is shot.

Here's a statement from Goldman: “Although Goldman Sachs held various positions in residential mortgage-related products in 2007, our short positions were not a ‘bet against our clients.’”

Yikes. This worse than I thought. Are they really going to use the “I didn't know the gun was loaded” defense?

Here's a clip from an article by Gretchen Morgenson and Louise Story in the New York Times which explains what Goldman was up to:

“Goldman and other firms eventually used the C.D.O.'s to place unusually large negative bets that were not mainly for hedging purposes, and investors and industry experts say that put the firms at odds with their own clients' interests.

“The simultaneous selling of securities to customers and shorting them because they

believed they were going to default is the most cynical use of credit information that I have ever seen,” said Sylvain R. Raynes, an expert in structured finance at R & R Consulting in New York. “When you buy protection against an event that you have a hand in causing, you are buying fire insurance on someone else’s house and then committing arson”

In early 2005, a group of prominent traders met at Deutsche Bank’s office in New York and drew up a new system, called Pay as You Go. This meant the insurance for those betting against mortgages would pay out more quickly....Other changes also increased the likelihood that investors would suffer losses if the mortgage market tanked.

Banks also set up ever more complex deals that favored those betting against C.D.O.’s.....At Goldman, Mr. Egot structured some Abacus deals in a way that enabled those betting on a mortgage-market collapse to multiply the value of their bets, to as much as six or seven times the face value of those C.D.O.’s. When the mortgage market tumbled, this meant bigger profits for Goldman and other short sellers — and bigger losses for other investors.” (“Banks Bundled Bad Debt, Bet Against It and Won”, Gretchen Morgenson and Louise Story, New York Times)

That sums it up, doesn’t it? Goldman is a serial arsonist. Here’s a passage from the Goldman Sales Primer:

Rule #1-Burn the client

Rule#2-Laugh all the way to the bank

Rule#3-Deny everything.

Of course, when the SEC lowered the boom on Friday, everyone at CNBC (the business channel) went into mourning. The moaning and groaning persisted all day. All the cliches about “intrusive government” and the “chilling” effect this would have on the markets, were dusted off and reiterated with religious solemnity. Jim Cramer, “Mad Money’s” blabbering fuckhead , defended Goldman saying the victims should have known what was going on. “Caveat emptor”, proclaimed Cramer. Buyer beware! If you get reamed, it’s your fault. Fortunately, the SEC doesn’t see it that way. Goldman’s defrauded its clients and now Goldman must pay. Expect a mile-long oil-slick of well-dressed lawyers winding-away from Goldman’s downtown offices on Monday.

Fabrice Tourre, is the Goldman vice president who is at the center of the controversy. He describes himself as the “fabulous Fab”, and appears to be a likable goofball who performed his duties like he was playing a video game. He was main engineer of the Frankenstein CDO that did all the damage. Unfortunately, for fabulous Fab, he left behind a damning paper-trail of what he was up to. Here’s the e mail that grabbed the attention of the SEC:

“More and more leverage in the system, The whole building is about to collapse anytime now...Only potential survivor, the fabulous Fab...standing in the middle of all these complex, highly leveraged, exotic trades he created without necessarily understanding all of the implications of those monstrosities!!!”

Right. So it’s all fun-and-games for V.P. Numskull. At least this leaves open the “insanity defense”. Keep in mind, these are supposed to be “the smartest guys in the room”. Small room. Here’s a clip from the Wall Street Journal:

“Early in the year, Mr. Tourre—began structuring Abacus, a new structured product to be made up of a collection of risky home loans.....

Dozens of deals like Abacus were packaged over the course of several years, said people familiar with the matter. Structured products had become so successful, in fact, that in 2008, Mr. Tourre moved to the firm’s London office to help launch the same business in Europe.” (“Trader Seized on Mortgage-Security Boom” Wall Street Journal)

Sure, screwing people is a “growth industry”. And a big organization like Goldman has a reservoir full of snakeoil, so it doesn’t have to worry about running-low on reserves. Just stitch-together a bunch of junk securities, dress them up in sequins and gold-lame’, dump them off on investors, and rake in big profits when the ship sinks. Wash, rinse, repeat. Tourre knew his job and did it well. The fault doesn’t lie with him. This goes all the way to the top, CEO Lloyd Blankfein, the man in the wheelhouse directing traffic. That’s where the buck stops.

But don’t count your chickens too soon. This whole matter smacks of politics bigtime. Obama probably just wants to push his financial reform bill across the finish line and is beating up on Goldman to get the public fired up. In fact, that’s probably what it is; just a bit of political step-dancing to build support for his agenda. Might as well put away those orange jumpsuits for now. It’s all theater.

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