Back to The Great American Bubble Machine

The Great American Bubble Machine

Matt Taibbi on how Goldman Sachs has engineered every major market manipulation since the Great Depression

MATT TAIBBI

Posted Jul 02, 2009 8:38 AM

In Rolling Stone Issue 1082-83, Matt Taibbi takes on "the Wall Street Bubble Mafia" — investment bank Goldman Sachs. The piece has generated controversy, with Goldman Sachs firing back that Taibbi's piece is "an hysterical compilation of conspiracy theories" and a spokesman adding, "We reject the assertion that we are inflators of bubbles and profiteers in busts, and we are painfully conscious of the importance in being a force for good." Taibbi shot back: "Goldman has its alumni pushing its views from the pulpit of the U.S. Treasury, the NYSE, the World Bank, and numerous other important posts; it also has former players fronting major TV shows. They have the ear of the president if they want it." Here, now, are excerpts from Matt Taibbi's piece and video of Taibbi exploring the key issues.

Matt Taibbi On Goldman Sachs' Big Scam

From Matt Taibbi's "The Great American Bubble Machine" in Rolling Stone Issue 1082-83.

The first thing you need to know about Goldman Sachs is that it's everywhere. The world's most powerful investment bank is a great vampire squid wrapped around the face of humanity, relentlessly jamming its blood funnel into anything that smells like money.

Any attempt to construct a narrative around all the former Goldmanites in influential positions quickly becomes an absurd and pointless exercise, like trying to make a list of everything. What you need to know is the big picture: If America is circling the drain, Goldman Sachs has found a way to be that drain — an extremely unfortunate loophole in the system of Western democratic capitalism, which never foresaw that in a society governed passively by free markets and free elections, organized greed always defeats disorganized democracy.

They achieve this using the same playbook over and over again. The formula is relatively simple: Goldman positions itself in the middle of a speculative bubble, selling investments they know are crap. Then they hoover up vast sums from the middle and lower floors of society with the aid of a crippled and corrupt state that allows it to rewrite the rules in exchange for the relative pennies the bank throws at political patronage. Finally, when it all goes bust, leaving millions of ordinary citizens broke and starving, they begin the entire process over again, riding in to rescue us all by lending us back our own money at interest, selling themselves as men above greed, just a bunch of really smart guys keeping the wheels greased. They've been pulling this same stunt over and over since the 1920s — and now they're preparing to do it again, creating what may be the biggest and most audacious bubble yet.

NEXT: Goldman Sachs' Role in the Housing and Internet Busts

From Matt Taibbi's "The Great American Bubble Machine" in Rolling Stone Issue 1082-83.

The basic scam in the Internet Age is pretty easy even for the financially illiterate to grasp. Companies that weren't much more than pot-fueled ideas scrawled on napkins by up-too-late bong-smokers were taken public via IPOs, hyped in the media and sold to the public for megamillions. It was as if banks like Goldman were wrapping ribbons around watermelons, tossing them out 50-story windows and opening the phones for bids. In this game you were a winner only if you took your money out before the melon hit the pavement.

It sounds obvious now, but what the average investor didn't know at the time was that the banks had changed the rules of the game, making the deals look better than they actually were. They did this by setting up what was, in reality, a two-tiered investment system — one for the insiders who knew the real numbers, and another for the lay investor who was invited to chase soaring prices the banks themselves knew were irrational. While Goldman's later pattern would be to capitalize on changes in the regulatory environment, its key innovation in the Internet years was to abandon its own industry's standards of quality control.

Goldman's role in the sweeping global disaster that was the housing bubble is not hard to trace. Here again, the basic trick was a decline in underwriting standards, although in this case the standards weren't in IPOs but in mortgages. By now almost everyone knows that for decades mortgage dealers insisted that home buyers be able to produce a down payment of 10 percent or more, show a steady income and good credit rating, and possess a real first and last name. Then, at the dawn of the new millennium, they suddenly threw all that shit out the window and started writing mortgages on the backs of napkins to cocktail waitresses and ex-cons carrying five bucks and a Snickers bar.

And what caused the huge spike in oil prices? Take a wild guess. Obviously Goldman had help — there were other players in the physical-commodities market — but the root cause had almost everything to do with the behavior of a few powerful actors determined to turn the once-solid market into a speculative casino. Goldman did it by persuading pension funds and other large institutional investors to invest in oil futures — agreeing to buy oil at a certain price on a fixed date. The push transformed oil from a physical commodity, rigidly subject to supply and demand, into something to bet on, like a stock. Between 2003 and 2008, the amount of speculative money in commodities grew from $13 billion to $317 billion, an increase of 2,300 percent. By 2008, a barrel of oil was traded 27 times, on average, before it was actually delivered and consumed.

NEXT: Goldman Sachs Graduates in the Government

From Matt Taibbi's "The Great American Bubble Machine" in Rolling Stone Issue 1082-83.

The history of the recent financial crisis, which doubles as a history of the rapid decline and fall of the suddenly swindled-dry American empire, reads like a Who's Who of Goldman Sachs graduates. By now, most of us know the major players. As George Bush's last Treasury secretary, former Goldman CEO Henry Paulson was the architect of the bailout, a suspiciously self-serving plan to funnel trillions of Your Dollars to a handful of his old friends on Wall Street. Robert Rubin, Bill Clinton's former Treasury secretary, spent 26 years at Goldman before becoming chairman of Citigroup — which in turn got a $300 billion taxpayer bailout from Paulson. There's John Thain, the asshole chief of Merrill Lynch who bought an $87,000 area rug for his office as his company was imploding; a former Goldman banker, Thain enjoyed a multibillion-dollar handout from Paulson, who used billions in taxpayer funds to help Bank of America rescue Thain's sorry company. And Robert Steel, the former Goldmanite head of Wachovia, scored himself and his fellow executives $225 million in golden-parachute payments as his bank was self-destructing. There's Joshua Bolten, Bush's chief of staff during the bailout, and Mark Patterson, the current Treasury chief of staff, who was a Goldman lobbyist just a year ago, and Ed Liddy, the former Goldman director whom Paulson put in charge of bailed-out insurance giant AIG, which forked over $13 billion to Goldman after Liddy came on board. The heads of the Canadian and Italian national banks are Goldman alums, as is the head of the World Bank, the head of the New York Stock Exchange, the last two heads of the Federal Reserve Bank of New York — which, incidentally, is now in charge of overseeing Goldman.

But then, something happened. It's hard to say what it was exactly; it might have been the fact that Goldman's co-chairman in the early Nineties, Robert Rubin, followed Bill Clinton to the White House, where he directed the National Economic Council and eventually became Treasury secretary. While the American media fell in love with the story line of a pair of baby-boomer, Sixties-child, Fleetwood Mac yuppies nesting in the White House, it also nursed an undisguised crush on Rubin, who was hyped as without a doubt the smartest person ever to walk the face of the Earth, with Newton, Einstein, Mozart and Kant running far behind.

Rubin was the prototypical Goldman banker. He was probably born in a $4,000 suit, he had a face that seemed permanently frozen just short of an apology for being so much smarter than you, and he exuded a Spock-like, emotion-neutral exterior; the only human feeling you could imagine him experiencing was a nightmare about being forced to fly coach. It became almost a national cliché that whatever Rubin thought was best for the economy — a phenomenon that reached its apex in 1999, when Rubin appeared on the cover of Time with his Treasury deputy, Larry Summers, and Fed chief Alan Greenspan under the headline the committee to save the world. And "what Rubin thought," mostly, was that the American economy, and in particular the financial markets, were over-regulated and needed to be set free. During his tenure at Treasury, the Clinton White House made a series of moves that would have drastic consequences for the global economy — beginning with Rubin's complete and total failure to regulate his old firm during its first mad dash for obscene short-term profits.

NEXT: Goldman Sachs' Powerful Influence

From Matt Taibbi's "The Great American Bubble Machine" in Rolling Stone Issue 1082-83.

After the oil bubble collapsed last fall, there was no new bubble to keep things humming — this time, the money seems to be really gone, like worldwide-depression gone. So the financial safari has moved elsewhere, and the big game in the hunt has become the only remaining pool of dumb, unguarded capital left to feed upon: taxpayer money. Here, in the biggest bailout in history, is where Goldman Sachs really started to flex its muscle.

It began in September of last year, when then-Treasury secretary Paulson made a momentous series of decisions. Although he had already engineered a rescue of Bear Stearns a few months before and helped bail out quasi-private lenders Fannie Mae and Freddie Mac, Paulson elected to let Lehman Brothers — one of Goldman's last real competitors — collapse without intervention. ("Goldman's superhero status was left intact," says market analyst Eric Salzman, "and an investment-banking competitor, Lehman, goes away.") The very next day, Paulson greenlighted a massive, $85 billion bailout of AIG, which promptly turned around and repaid $13 billion it owed to Goldman. Thanks to the rescue effort, the bank ended up getting paid in full for its bad bets: By contrast, retired auto workers awaiting the Chrysler bailout will be lucky to receive 50 cents for every dollar they are owed.

Immediately after the AIG bailout, Paulson announced his federal bailout for the financial industry, a $700 billion plan called the Troubled Asset Relief Program, and put a heretofore unknown 35-year-old Goldman banker named Neel Kashkari in charge of administering the funds. In order to qualify for bailout monies, Goldman announced that it would convert from an investment bank to a bank-holding company, a move that allows it access not only to $10 billion in TARP funds, but to a whole galaxy of less conspicuous, publicly backed funding — most notably, lending from the discount window of the Federal Reserve. By the end of March, the Fed will have lent or guaranteed at least $8.7 trillion under a series of new bailout programs — and thanks to an obscure law allowing the Fed to block most congressional audits, both the amounts and the recipients of the monies remain almost entirely secret.

Converting to a bank-holding company has other benefits as well: Goldman's primary supervisor is now the New York Fed, whose chairman at the time of its announcement was Stephen Friedman, a former co-chairman of Goldman Sachs. Friedman was technically in violation of Federal Reserve policy by remaining on the board of Goldman even as he was supposedly regulating the bank; in order to rectify the problem, he applied for, and got, a conflict-of-interest waiver from the government. Friedman was also supposed to divest himself of his Goldman stock after Goldman became a bank-holding company, but thanks to the waiver, he was allowed to go out and buy 52,000 additional shares in his old bank, leaving him $3 million richer. Friedman stepped down in May, but the man now in charge of supervising Goldman — New York Fed president William Dudley — is yet another former Goldmanite.

The collective message of all of this — the AIG bailout, the swift approval for its bank-holding conversion, the TARP funds — is that when it comes to Goldman Sachs, there isn't a free market at all. The government might let other players on the market die, but it simply will not allow Goldman to fail under any circumstances. Its edge in the market has suddenly become an open declaration of supreme privilege. "In the past it was an implicit advantage," says Simon Johnson, an economics professor at MIT and former official at the International Monetary Fund, who compares the bailout to the crony capitalism he has seen in Third World countries. "Now it's more of an explicit advantage."

NEXT: Goldman Sachs' Excuse

From Matt Taibbi's "The Great American Bubble Machine" in Rolling Stone Issue 1082-83.

Fast-forward to today. It's early June in Washington, D.C. Barack Obama, a popular young politician whose leading private campaign donor was an investment bank called Goldman Sachs — its employees paid some $981,000 to his campaign — sits in the White House. Having seamlessly navigated the political minefield of the bailout era, Goldman is once again back to its old business, scouting out loopholes in a new government-created market with the aid of a new set of alumni occupying key government jobs.

Gone are Hank Paulson and Neel Kashkari; in their place are Treasury chief of staff Mark Patterson and CFTC chief Gary Gensler, both former Goldmanites. (Gensler was the firm's co-head of finance.) And instead of credit derivatives or oil futures or mortgage-backed CDOs, the new game in town, the next bubble, is in carbon credits — a booming trillion- dollar market that barely even exists yet, but will if the Democratic Party that it gave $4,452,585 to in the last election manages to push into existence a groundbreaking new commodities bubble, disguised as an "environmental plan," called cap-and-trade. The new carbon-credit market is a virtual repeat of the commodities-market casino that's been kind to Goldman, except it has one delicious new wrinkle: If the plan goes forward as expected, the rise in prices will be government-mandated. Goldman won't even have to rig the game. It will be rigged in advance.