People aren't really needed for anything else in the Griftopia, but since Americans require the illusion of self-government, we have elections.

To make sure those elections are effectively meaningless as far as Wall Street is concerned, two things end up being true. One is that voters on both sides of the aisle are gradually weaned off that habit of having real expectations for their politicians, consuming the voting process entirely as culture-war entertainment. The other is that millions of tenuously middle-class voters are conned into pushing Wall Street's own twisted greed ethos as though it were their own. The Tea Party, with its weirdly binary view of society as being split up cleanly into competing groups of producers and parasites—that's just a cultural echo of the insane greed-is-good belief system on Wall Street that's provided the foundation/excuse for a generation of brilliantly complex thievery. Those beliefs have trickled down to the ex-middle-class suckers struggling to stay on top of their mortgages and their credit card bills, and the real joke is that these voters listen to CNBC and Fox and they genuinely believe *they're* the producers in this binary narrative. They don't get that somewhere way up above, there's a group of people who've been living the Atlas dream for real—and building a self-dealing financial bureaucracy in their own insane image.

2

The Biggest Asshole in the Universe

Bad political systems on their own don't always make societies fail. Sometimes what's required for a real social catastrophe is for one or two ingeniously obnoxious individuals to rise to a position of great power—get a one-in-a-billion asshole in the wrong job and a merely unfair system of government suddenly turns into seventies Guatemala, the Serbian despotate, the modern United States.

Former Federal Reserve chief Alan Greenspan is that one-in-a-billion asshole who made America the dissembling mess that it is today. If his achievements were reversed, if this gnomish bug-eyed party crasher had managed to convert his weird social hang-ups into positive accomplishments, then today we'd be calling his career one of the greatest political fairy tales ever witnessed, an unlikeliest of ugly ducklings who through sheer pluck, cunning, and determination made it to the top and changed the world forever.

But that isn't what happened. Greenspan's rise is instead a tale of a gerbilish mirror-gazer who flattered and bullshitted his way up the Matterhorn of American power and then, once he got to the top, feverishly jacked himself off to the attentions of Wall Street for twenty consecutive years—in the process laying the intellectual foundation for a generation of orgiastic greed and overconsumption and turning the Federal Reserve into a permanent bailout mechanism for the super-rich.

Greenspan was also the perfect front man for the hijacking of the democratic process that took place in the eighties, nineties, and the early part of the 2000s. During that time political power gradually shifted from the elected government to private and semiprivate institutions run by unelected officials whose sympathies were with their own class rather than any popular constituency. We suffered a series of economic shocks over the course of those years, and the official response from the institutions subtly pushed the country's remaining private wealth to one side while continually shifting the risk and the loss to the public.

This profoundly focused effort led to an intense concentration of private wealth on the one hand and the steady disenfranchisement of the average voter and the taxpayer on the other (who advanced inexorably, headfirst, into the resultant debt). But the true genius of this blunt power play was that it was cloaked in a process that everyone who mattered agreed to call the apolitical, "technocratic" stewardship of the economy.

Greenspan was the deadpan figurehead who as head of the "apolitical" Federal Reserve brilliantly played the part of that impartial technocrat. His impartiality was believable to the public precisely because of his long-demonstrated unscrupulousness and political spinelessness: he sucked up with equal ferocity to presidents of both parties and courted pundit-admirers from both sides of the editorial page, who all blessed his wrinkly pronouncements as purely nonpartisan economic wisdom.

Greenspan's rise to the top is one of the great scams of our time. His career is the perfect prism through which one can see the twofold basic deception of American politics: a system that preaches sink-or-swim laissez-faire capitalism to most but acts as a highly interventionist, bureaucratic welfare state for a select few. Greenspan pompously preached ruthless free-market orthodoxy every chance he got while simultaneously using all the powers of the state to protect his wealthy patrons from those same market forces. A perfectly two-faced man, serving a perfectly two-faced state. If you can see through him, the rest of it is easy.

Greenspan was born in 1926, just before the Depression, and boasts a background that reads a little like a generational prequel to the life of Woody Allen—a middle-class Jewish New Yorker from the outer rings of the city, a gaggle-eyed clarinet player who worshipped the big bands, used radio as an escape, obsessed over baseball heroes, and attended NYU (the latter with more success than Woody), eventually entering society in a state of semipanicked indecision over what career to pursue.

In his writings Greenspan unapologetically recalls being overwhelmed as a young man by the impression left by his first glimpses of the upper classes and the physical trappings of their wealth. In his junior year of college he had a summer internship at an investment bank called Brown Brothers Harriman:*

> Prescott Bush, father of George H. W. Bush and grandfather of George W. Bush, served there as a partner before and after his tenure in the U.S. Senate. The firm was literally on Wall Street near the stock exchange and the morning I went to see Mr. Banks was the first time I'd ever set foot in such a place. Walking into these offices, with their gilded ceilings and rolltop desks and thick carpets, was like entering a sanctum of venerable wealth—it was an awesome feeling for a kid from Washington Heights.

*Note the name-dropping at the start of this quote, a literary habit that through the years has infected Greenspan's writings and speeches like the world's most persistent case of herpes. His autobiography, *The Age of Turbulence,* features numerous passages in which his lists of dropped names ramble on with feverish, almost Gogolian intensity. Take for instance this one, in which he talks of the fiftieth birthday party his girlfriend Barbara Walters threw for him: "The guests were the people I'd come to think of as my New York friends: Henry and Nancy Kissinger, Oscar and Annette de la Renta, Felix and Liz Rohatyn, Brooke Astor (I knew her as a kid of seventy-five), Joe and Estée Lauder, Henry and Louise Grunwald, 'Punch' and Carol Sulzberger, and David Rockefeller." Needless to say, when the Federal Reserve Act was passed in 1913, Congress was probably not imagining that America would ultimately hire a central banker who dated anchorwomen and bragged about hanging out with Oscar de la Renta. Greenspan has always appeared constitutionally incapable of not letting people know who his friends are—it's always seemed to be a matter of tremendous importance to him—which is why it's absolutely reasonable to wonder if maybe that was a reason his Fed policies were so much more popular with the Hamptons set than those of a notoriously shabby recluse like Paul Volcker.

Greenspan left NYU to pursue a doctorate in economics at Columbia University, where one of his professors was economist Arthur Burns, a fixture in Republican administrations after World War II who in 1970 became chief of the Federal Reserve. Burns would be Greenspan's entrée into several professional arenas, most notably among the Beltway elite.

Remarkably, Greenspan's other great career rabbi was the objectivist novelist Ayn Rand, an antigovernment zealot who was nearly the exact ideological opposite of a career bureaucrat like Burns.

Greenspan met Rand in the early fifties after leaving Columbia, attending meetings at Rand's apartment with a circle of like-minded intellectual jerk-offs who called themselves by the ridiculous name the "Collective" and who provided Greenspan the desired forum for social ascent.

These meetings of the "Collective" would have an enormous impact on American culture by birthing a crackpot antitheology dedicated to legitimizing relentless self-interest—a grotesquerie called objectivism that hit the Upper East Side cocktail party circuit hard in the fifties and sixties.

It is important to spend some time on the seriously demented early history of objectivism, because this lunatic religion that should have choked to death in its sleep decades ago would go on, thanks in large part to Greenspan, to provide virtually the entire intellectual context for the financial disasters of the early twenty-first century.

Rand, the Soviet refugee who became the archpriestess of the movement, was first of all a perfect ancillary character in the black comedy that is Greenspan's life—a bloviating, arbitrary, self-important pseudo-intellectual who recalls the gibberish-spewing academic twits in Woody Allen spoofs like "No Kaddish for Weinstein" and "My Speech to the Graduates." In fact, some of Rand's quirks seemed to have been pulled more or less directly from Allen's movies; her dictatorial stance on facial hair ("She . . . regarded anyone with a beard or a mustache as inherently immoral," recalled one Rand friend) could have fit quite easily in the mouth of the Latin despot Vargas in *Bananas,* who demanded that his subjects change their underwear once an hour.

A typical meeting of Rand's Collective would involve its members challenging one another to prove they exist. "How do you explain the

fact that you're here?" one Collective member recalls asking Greenspan. "Do you require anything besides the proof of your own senses?"

Greenspan played along with this horseshit and in that instance reportedly offered a typically hedging answer. "I think that I exist. But I don't know for sure," he reportedly said. "Actually, I can't say for sure that anything exists." (The Woody Allen version would have read, "I can't say for sure that I exist, but I do know that I have to call two weeks in advance to get a table at Sardi's.")

One of the defining characteristics of Rand's clique was its absolutist ideas about good and evil, expressed in a wildly off-putting, uncompromisingly bombastic rhetoric that almost certainly bled downward to the group ranks from its Russian émigré leader, who might have been one of the most humor-deprived people ever to walk the earth.

Rand's book *Atlas Shrugged,* for instance, remains a towering monument to humanity's capacity for unrestrained self-pity—it's a bizarre and incredibly long-winded piece of aristocratic paranoia in which a group of Randian supermen decide to break off from the rest of society and form a pure free-market utopia, and naturally the parasitic lower classes immediately drown in their own laziness and ineptitude.

The book fairly gushes with the resentment these poor "Atlases" (they are shouldering the burdens of the whole world!) feel toward those who try to use "moral guilt" to make them share their wealth. In the climactic scene the Randian hero John Galt sounds off in defense of self-interest and attacks the notion of self-sacrifice as a worthy human ideal in a speech that lasts *seventy-five pages.*

It goes without saying that only a person possessing a mathematically inexpressible level of humorless self-importance would subject anyone to a seventy-five-page speech about anything. Hell, even Jesus Christ barely cracked two pages with the Sermon on the Mount. Rand/Galt manages it, however, and this speech lays the foundation of objectivism, a term that was probably chosen because "greedism" isn't catchy enough.

Rand's rhetorical strategy was to create the impression of depth through overwhelming verbal quantity, battering the reader with a relentless barrage of meaningless literary curlicues. Take this bit from Galt's famous speech in *Atlas Shrugged*:

> Rationality is the recognition of the fact that existence exists, that nothing can alter the truth and nothing can take precedence over that act of perceiving it, which is thinking—that the mind is one's only judge of values and one's only guide of action—that reason is an absolute that permits no compromise—that a concession to the irrational invalidates one's consciousness and turns it from the task of perceiving to the task of faking reality—that the alleged short-cut to knowledge, which is faith, is only a short-circuit destroying the mind—that the acceptance of a mystical invention is a wish for the annihilation of existence and, properly, annihilates one's consciousness.

A real page-turner. Anyway, Alan Greenspan would later regularly employ a strikingly similar strategy of voluminous obliqueness in his public appearances and testimony before Congress. And rhetorical strategy aside, he would forever more cling on some level to the basic substance of objectivism, expressed here in one of the few relatively clear passages in *Atlas Shrugged*:

> A living entity that regarded its means of survival as evil, would not survive. A plant that struggled to mangle its roots, a bird that fought to break its wings would not remain for long in the existence they affronted. But the history of man has been a struggle to deny and to destroy his mind . . .
>
> Since life requires a specific course of action, any other course will destroy it. A being who does not hold his own life as the motive and goal of his actions, is acting on the motive and standard of *death*. Such a being is a metaphysical monstrosity, struggling to oppose, negate and contradict the fact of his own existence, running blindly amuck on a trail of destruction, capable of nothing but pain.

This is pure social Darwinism: self-interest is moral, interference (particularly governmental interference) with self-interest is evil, a fancy version of the Gordon Gekko pabulum that "greed is good." When you dig deeper into Rand's philosophy, you keep coming up with more of the same.

Rand's belief system is typically broken down into four parts: metaphysics (objective reality), epistemology (reason), ethics (self-interest), and politics (capitalism). The first two parts are basically pure bullshit and fluff. According to objectivists, the belief in "objective reality" means that "facts are facts" and "wishing" won't make facts change. What it actually means is "When I'm right, I'm right" and "My facts are facts and your facts are not facts."

This belief in "objective reality" is what gives objectivists their characteristic dickish attitude: since they don't really believe that facts look different from different points of view, they don't feel the need to question themselves or look at things through the eyes of others. Since being in tune with how things look to other people is a big part of that magical unspoken connection many people share called a sense of humor, the "metaphysics" of objectivism go a long way toward explaining why there has never in history been a funny objectivist.

The real meat of Randian thought (and why all this comes back to Greenspan) comes in their belief in self-interest as an ethical ideal and pure capitalism as the model for society's political structure. Regarding the latter, Randians believe government has absolutely no role in economic affairs; in particular, government should never use "force" except against such people as criminals and foreign invaders. This means no taxes and no regulation.

To sum it all up, the Rand belief system looks like this:

1. Facts are facts: things can be absolutely right or absolutely wrong, as determined by reason.
2. According to my reasoning, I am absolutely right.
3. Charity is immoral.
4. Pay for your own fucking schools.

Rand, like all great con artists, was exceedingly clever in the way she treated the question of how her ideas would be employed. She used a strategic vagueness that allowed her to paper over certain uncomfortable contradictions. For instance, she denounced tax collection as a use of "force" but also quietly admitted the need for armies and law enforcement, which of course had to be paid for somehow. She denounced the very idea of government interference in economic affairs but also here and there conceded that fraud and breach of contract were crimes of "force" that required government intervention.

She admitted all of this, but her trick was one of emphasis. Even as she might quietly admit to the need for *some* economic regulation, for the most part when she talked about "crime" and "force" she either meant (a) armed robbers or pickpockets or (b) governments demanding taxes to pay for social services:

> Be it a highwayman who confronts a traveler with the ultimatum: "Your money or your life," or a politician who confronts a country with the ultimatum: "Your children's education or your life," the meaning of that ultimatum is: "Your mind or your life."

A conspicuous feature of Rand's politics is that they make absolutely perfect sense to someone whose needs are limited to keeping burglars and foreign communists from trespassing on their Newport manses, but none at all to people who might want different returns for their tax dollar. Obviously it's true that a Randian self-made millionaire can spend money on private guards to protect his mansion from B-and-E artists. But exactly where do the rest of us look in the Yellow Pages to hire private protection against insider trading? Against price-fixing in the corn and gasoline markets? Is each individual family supposed to hire Pinkertons to keep the local factory from dumping dioxin in the county reservoir?

Rand's answer to all of these questions was to ignore them. There were no two-headed thalidomide flipper-babies in Rand's novels, no Madoff scandals, no oil bubbles. There *were,* however, a lot of lazy-ass poor people demanding welfare checks and school taxes. It was belief in this simplistic black-and-white world of pure commerce and blood-sucking parasites that allowed Rand's adherents to present themselves as absolutists, against all taxes, all regulation, and all government interference in private affairs—despite the fact that all of these ideological absolutes quietly collapsed whenever pragmatic necessity required it. In other words, it was incoherent and entirely subjective. Its rhetoric flattered its followers as Atlases with bottomless integrity, but the fine print allowed them to do whatever they wanted.

This slippery, self-serving idea ended up being enormously influential in mainstream American politics later on. There would be constant propaganda against taxes and spending and regulation as inherent evils, only these ideas would often end up being quietly ignored when there was a need for increased military spending, bans on foreign drug reimportation, FHA backing for mortgage lenders, Overseas Private Investment Corporation loans, or other forms of government largesse or interference for the right people. American politicians reflexively act as perfectly Randian free-market, antitax purists (no politician beyond the occasional Kucinich will admit to any other belief system) except when, quietly and behind the scenes, they don't.

The person of Alan Greenspan was where this two-sided worldview first became a polished political innovation. He was able to play the seemingly incompatible roles of believer and pragmatist fluidly; there were no core beliefs in there to gum up the works. It's not hard to imagine that even as Greenspan sat in Rand's apartment cheerfully debating the proofs of his own existence, he was inwardly cognizant of what complete goofballs his friends were, how quickly their absolutist dictums would wilt in actual practice. One of the surest proofs of this is Greenspan's schizophrenic posture toward his future employer, the Federal Reserve System.

Rand's objectivists were very strongly opposed to the very concept of the Federal Reserve, a quasi-public institution created in 1913 that allowed a federally appointed banking official—the Federal Reserve chairman—to control the amount of money in the economy.

When he was at Rand's apartment, Greenspan himself was a staunch opponent of the Federal Reserve. One of Rand's closest disciples, Nathaniel Branden, recalled Greenspan's feelings about the Fed. "A number of our talks centered on the Federal Reserve Board's role in influencing the economy by manipulating the money supply," Branden recalled. "Greenspan spoke with vigor and intensity about a totally free banking system."

Throughout the fifties and sixties Greenspan adhered strictly to

Rand's beliefs. His feelings about the Federal Reserve during this time are well documented. In 1966 he wrote an essay called "Gold and Economic Freedom" that blamed the Fed in part for the Great Depression:

> The excess credit which the Fed pumped into the economy spilled over into the stock market—triggering a fantastic speculative boom.

Foreshadowing alert! In any case, during this same period Greenspan drew closer to Rand, who as self-appointed pope of the protocapitalist religion had become increasingly unhinged, prone to Galtian rants and banishments. One of her rages centered around Branden, a handsome and significantly younger psychotherapist Rand met when she was forty-four and Branden was nineteen. The two had an affair despite the fact that both were married; in a cultist echo of David Koresh/Branch Davidian sexual ethics, both spouses reportedly consented to the arrangement to keep the movement leader happy.

But in 1968, eighteen years into their relationship, Rand discovered that Branden had used his pure reason to deduce that a young actress named Patrecia Scott was, objectively speaking, about ten thousand times hotter than the by-then-elderly and never-all-that-pretty-to-begin-with Rand, and was having an affair with her without Rand's knowledge.

Rand then used *her* pure reason and decided to formally banish both Branden and his wife, Barbara, from the movement for "violation of objectivist principles." This wouldn't be worth mentioning but for the hilarious fact that Greenspan signed the excommunication decree, which read:

> Because Nathaniel Branden and Barbara Branden, in a series of actions, have betrayed fundamental principles of Objectivism, we condemn and repudiate these two persons irrevocably.

The irony of a refugee from Soviet tyranny issuing such a classically Leninist excommunication appears to have been completely lost on Rand. But now here comes the really funny part. Almost exactly simultaneous to his decision to sign this preposterous decree, Greenspan did

something that was anathema to any good Randian's beliefs: he went to work for a politician.

In 1968 he joined the campaign of Richard Nixon, going to work as an adviser on domestic policy questions. He then worked for Nixon's Bureau of the Budget during the transition, after Nixon's victory over Humphrey. This was a precursor to an appointment to serve on Gerald Ford's Council of Economic Advisers in 1974; he later ingratiated himself into the campaign of Ronald Reagan in 1980, served on a committee to reform Social Security, and ultimately went on to become Federal Reserve chief in 1987. There is a whole story about Greenspan's career as a private economist that took place in the intervening years, but for now the salient fact about Greenspan is that this is a person who grew up in an intellectual atmosphere where collaboration with the government in any way was considered a traitorous offense, but who nonetheless spent most of his adult life involved in government in one way or another. He told the *New York Times Magazine* in 1976 that he rationalized his decision to join the government thusly: "I could have a real effect."

Toward the end of her life, even Rand began to wonder about Greenspan's commitment to the faith, leading to one of the few genuinely salient observations she ever made in her whole silly life: "I think that Alan basically is a social climber," she said.

This ability to work both sides of the aisle at the same time would ultimately amaze even Barbara Walters, whom Greenspan somehow managed to make his girlfriend in the seventies. "How Alan Greenspan, a man who believed in the philosophy of little government interference and few rules of regulation, could end up becoming chairman of the greatest regulatory agency in the country is beyond me," Walters said in 2008.

How did it happen? Among other things, Alan Greenspan was one of the first Americans to really understand the nature of celebrity in the mass-media age. Thirty years before Paris Hilton, Greenspan managed to become famous for being famous—and levered that skill into one of the most powerful jobs on earth.

Alan Greenspan's political career was built on a legend—the legend of the ultimate Wall Street genius, the Man with All the Answers. But the legend wasn't built on his actual performance as an economist. It was a reputation built on a reputation. In fact, if you go back and look at his rise now, his career path has a lot less in common with economist icons like Keynes or Friedman than it does with celebrity con artists like L. Ron Hubbard, Tony Robbins, or Beatles guru Maharishi Mahesh Yogi.

Like the Maharishi, Greenspan got his foot in the big door by dazzling deluded celebrities with voluble pseudo-mystical nonsense. One of his big breaks came when a lawyer named Leonard Garment introduced him to Dick Nixon in 1968.

Garment would later describe Greenspan's bloviating on economic matters in that meeting as "Nepal Kathmandu language." Nixon, nonetheless, was impressed, saying, "That's a very intelligent man." Later he brought him into the campaign. And although Greenspan eventually declined a formal role in Nixon's government, he would henceforth thrive in a role as economic guru to men with power, a role that the press somehow never failed to be made aware of.

When he finally did come into government full-time as head of Ford's Council of Economic Advisers, glowing accounts of Greenspan's authority in the White House routinely appeared in the press.

"Greenspan has a unique relationship with the president," crowed *BusinessWeek,* which added that, according to one aide, "on economic policy, Alan is a heavyweight." Future right-wing Godzilla Dick Cheney, then serving as Ford's chief of staff, added in the *New York Times Magazine* that President Ford attached "more weight to Greenspan's views than those of any other among his economic advisers."

Sometimes Greenspan himself was the source of the compliments. The *New Yorker* in 1974, addressing the inflation issue that was hot at the time, offered this hilarious piece of praise: "Economists of all persuasions (with the exception of Alan Greenspan, an Ayn Rand disciple, who heads the President's Council of Economic Advisers) admit to being baffled by today's problems."

Not long after that, in 1975, Greenspan became the first economist to grace the cover of *Newsweek;* by then he had also already been named

to *Time's* illustrious Board of Economists, which met four times a year to harrumph about economic matters for the mag. Greenspan was even asked for an interview by *Penthouse* that same year, although he declined.

That Greenspan has always been intensely interested in press attention is something that virtually every source I spoke with accepts almost without question. His interest in the media can even be seen in his personal life; he dated in succession three different prominent television figures, moving from Barbara Walters in the late seventies to *MacNeil/Lehrer* producer Susan Mills in the eighties to the woman he ultimately married, NBC correspondent Andrea Mitchell.

One reporter for a major daily newspaper who covered the Fed in the nineties tells of getting frantic calls from Greenspan's office at 7:00 the morning after a negative piece appeared. "I was still half asleep, but the chairman was already unhappy," he said. Around the same time, Paul Weller, a University of Iowa professor who wrote a blisteringly critical paper on Greenspan, was hounded for a copy by Fed press aides before it was even published. "Alan himself wanted to see it," the author chuckles now.

Greenspan was exceptionally skilled at pushing his image of economic genius, particularly since his performance as an economic prognosticator was awful at best. "He was supposedly the smartest man in the world," laughs economist Brian Wesbury today. "He was the greatest, the Maestro. Only if you look at his record, he was wrong about almost everything he ever predicted."

Fed watchers and Greenspan critics all seem to share a passion for picking out which of Greenspan's erroneous predictions was most ridiculous. One of his most famous was his pronouncement in the *New York Times* in January 1973: "It's very rare that you can be as unqualifiedly bullish as you can now," he said. The market proceeded to lose 46 percent of its value over the next two years, plunging from above 1,000 the day of Greenspan's prediction to 571 by December 1974.

Greenspan was even bad at predicting events that had already happened. In April 1975, Greenspan told a New York audience that the recession wasn't over, that the "worst was yet to come." The economy swiftly improved, and the National Bureau of Economic Research later placed the end of the recession at March 1975, a month before Greenspan's speech.

Greenspan's career is full of such pronouncements. In July 1990, at the start of the recession that would ultimately destroy the presidency of George H. W. Bush, Greenspan opined: "In the very near term there's little evidence that I can see to suggest the economy is tilting over [into recession]." Months later, as the bad news continued, Greenspan soldiered on: "Those who argue that we are already in a recession I think are reasonably certain to be wrong."

By October, with the U.S. in the sixth of what would ultimately be ten consecutive months of job losses, Greenspan remained stubborn. "The economy," he said, "has not yet slipped into recession."

The economy has a lot in common with the weather, and even very good economists charged with the job of predicting market swings can become victims of unexpected turns, just like meteorologists. But Greenspan's errors were often historic, idiotic blunders, evidence of a fundamental misunderstanding of problems that led to huge disasters. In fact, if you dig under almost every one of the major financial crashes of our time, you can find some kind of Greenspan quote cheerfully telling people not to worry about where the new trends in the economy were leading.

Before the S&L crisis exploded Greenspan could be seen giving a breezy thumbs-up to now-notorious swindler Charles Keating, whose balance sheet Greenspan had examined—he said that Keating's Lincoln Savings and Loan "has developed a series of carefully planned, highly promising and widely diversified projects" and added that the firm "presents no foreseeable risk to the Federal Savings and Loan Corporation."

The mistake he made in 1994 was even worse. After a few (relatively) small-scale disasters involving derivatives of the sort that would eventually nearly destroy the universe in 2008, Greenspan told Congress that the risks involved with derivatives were "negligible," testimony that was a key reason the government left the derivatives market unregulated. His misreading of the tech bubble of the late nineties is legendary (more on that later); he also fell completely for the Y2K scare and at one point early in the George W. Bush presidency actually worried aloud that the national debt might be repaid too quickly.

But it wasn't Greenspan's economic skill that got him to the top banker job. Instead, it was his skill as a politician. During Ronald Reagan's first and second terms, while the irritatingly independent Paul Volcker sat on the Fed throne, Greenspan was quietly working the refs, attending as many White House functions as he could. Former Reagan aides told Greenspan's biographer Jerome Tuccille that "Alan made a point of regularly massaging the people who mattered." Another official, Martin Anderson, reported that "I don't think I was in the White House once where I didn't see him sitting in the lobby or working the offices. I was absolutely astounded by his omnipresence."

Greenspan had proved his worth to Reagan by using a commission he headed to perform one of the all-time budgetary magic tricks, an invisible tax hike that helped the supposedly antitax Reagan administration fund eight years of massive deficit spending.

In 1981 Reagan appointed Greenspan to head the National Commission on Social Security Reform, which had been created to deal with an alleged short-term funding crisis that would leave the Old-Age and Survivors Insurance Trust Fund bankrupt by 1983. It goes without saying that any political decision one makes with regard to Social Security is hazardous; cutting benefits is a shortcut to electoral death, and the alternative, raising taxes, isn't so palatable either.

Greenspan's solution was to recommend hikes in the Social Security tax, which of course is not considered a real "tax" (Reagan would hilariously later describe such hikes as "revenue enhancements") because the taxpayer theoretically gets that money back later on in benefits. The thinking here was that in the early eighties, with so many baby boomers now in their prime earning years, the Reagan administration would hike payments to build up a surplus that could in twenty or thirty years be used to pay out benefits when those same baby boomers reached retirement age. The administration accepted those proposals, and the Social Security tax rate went from 9.35 percent in 1981 to 15.3 percent by 1990.

Two things about this. One, Social Security taxes are very regressive, among other things because they only apply to wage income (if you're a hedge fund manager or a Wall Street investor and you make all your money in carried interest or capital gains, you don't pay) and they are also capped, at this writing at around $106,000, meaning that wages above a certain level are not taxed at all. That means that a married couple earning $100,000 total will pay roughly the same amount of Social Security taxes that Lloyd Blankfein or Bill Gates will (if not more, depending on how the latter two structure their compensation). So if you ignore the notion that Social Security taxes come back as benefits later on, and just think of them as a revenue source for the government, it's a way for the state to take money from working- and middle-class taxpayers at a highly disproportional rate.

Second, Greenspan's plan to build up a sort of Social Security war chest for use in paying out benefits to retirees twenty years down the road was based on a fallacy. When you pay money into Social Security, it doesn't go into a locked box that is separate from the rest of the budget and can't be used for other government spending. After the Greenspan reforms, the Social Security Administration bought T-bills with that money, essentially lending the cash back to the government for use in other appropriations. So if, let's say, your president wanted an extra few billion dollars or so of short-term spending money, he could just reach into the budget and take all that Social Security money, leaving whoever would be president two decades later holding not cash to pay out Social Security benefits, but government notes or bonds, i.e., IOUs.

And that's exactly what happened. The recommendations ushered in after Greenspan's commission effectively resulted in $1.69 trillion in new, regressive taxes over the next twenty years or so.

But instead of keeping their hands off that money and preserving it for Social Security payments, Reagan, Bush I, Clinton, and Bush II spent it—all of it—inspiring the so-called Social Security crisis of George W. Bush's presidency, in which it was announced suddenly that Social Security, far from having a surplus, was actually steaming toward bankruptcy. The bad news was released to the public by then–Treasury secretary Paul O'Neill, who let it slip that the Social Security fund had no assets at all, and instead just had pieces of paper in its account.

"I come to you as managing trustee of Social Security," O'Neill said. "Today we have no assets in the trust fund. We have the good faith and credit of the United States government that benefits will flow."

In other words, Greenspan and Reagan had conspired to hike Social Security payments, justifying it with the promise of building up a Social Security nest egg for subsequent decades, then used up that nest egg on current government spending.

Now, it was bad enough that Greenspan, who as a Randian was supposedly against all use of government "force," would propose such a big tax hike. But what made his role especially villainous was that when George W. Bush decided to start sounding alarm bells about the future of Social Security, it was none other than Alan Greenspan who came out and argued that maybe it was time to cut Social Security benefits. This is from a *Washington Post* story in February 2004:

> Greenspan offered several ways to curtail federal spending growth, including reducing Social Security and Medicare benefits. The Fed chairman again recommended raising the age at which retirees become eligible, to keep pace with the population's rising longevity. And he reminded lawmakers that they could link cost-of-living increases in benefits levels to a measure of inflation other than the consumer price index, a widely followed measure that some economists believe overstates the rise in overall prices. A measure that showed less inflation would cause benefit levels to rise more slowly.

To recap: Greenspan hikes Social Security taxes by a trillion and a half dollars or so, four presidents spend all that money on other shit (including, in George W. Bush's case, a massive tax cut for the wealthy), and then, when it comes time to start paying out those promised benefits, Greenspan announces that it can't be afforded, the money isn't there, benefits can't be paid out.

It was a shell game—money comes in the front door as payroll taxes and goes right out the back door as deficit spending, with only new payroll taxes over the years keeping the bubble from popping, continuing the illusion that the money had never left. Senator Daniel Patrick Moynihan, way back in 1983, had called this "thievery," but as the scam played out over the decades it earned a more specific title. "A classic Ponzi scheme" is how one reporter who covered Greenspan put it.

Coming up with a scheme like this is the sort of service that endears

Fed does,* so in the interests of sanity it's probably best to skip the long version and focus on its magical money-creating powers, the key to the whole bubble scam. The bank has a great many functions—among other things, it enforces banking regulations and maintains and standardizes the currency—but its most obvious and important job has to do with regulating the money supply.

The basic idea behind the Fed's regulation of the money supply is to keep the economy as healthy as possible by limiting inflation on the one hand and preventing recession on the other. It achieves this by continually expanding and contracting the amount of money in the economy, theoretically tightening when there is too much buying and inflation and loosening when credit goes slack and the lack of lending and business stimulation threatens recession.

The Fed gets its pseudo-religious aura from its magical ability to create money out of nothing, or to contract the money supply as it sees fit. As a former Boston Fed chief named Richard Syron has pointed out, the bank has even fashioned its personnel structure to resemble that of the Catholic Church, with a pope (the chairman), cardinals (the regional governors), and a curia (the senior staff).

One way that money is created is through new issuance of private credit; when private banks issue new loans, they essentially create money out of thin air. The Fed supervises this process and theoretically monitors the amount of new loans issued by the banks. It can raise or lower the amount of new loans by raising or lowering margin requirements, i.e., the number of hard dollars each bank has to keep on hand every time it makes a loan. If the margin requirement is 10 percent, banks have to keep one dollar parked in reserve at the Fed for every ten they lend out. If the Fed feels like increasing the amount of money in circulation, it can lower the margin rate to, say, 9 percent, allowing banks to lend out about eleven dollars for every one kept in reserve at the Fed.

The bank can also inject money into the system directly, mainly through two avenues. One is by lending money directly to banks at a

*It's a heavy subject even in the literal sense. One of the definitive works on the Fed, William Greider's *Secrets of the Temple*, is such a legendarily dense and physically massive book that a group of editors I know jokingly dared one another to try to shoplift it.

thing called the *discount window*, which allows commercial banks to borrow from the Fed at relatively low rates to cover short-term financing problems.

The other avenue is for the Fed to buy Treasury bills or bonds from banks or brokers. It works like this: The government, i.e., the Treasury, decides to borrow money. One of a small group of private banks called *primary dealers* is contracted to raise that money for the Treasury by selling T-bills or bonds or notes on the open market. Those primary dealers (as of this writing there are eighteen of them, all major institutions, including Goldman Sachs, Morgan Stanley, and Deutsche Bank) on occasion sell those T-bills to the Fed, which simply credits that dealer's account when it buys the securities. Through this circular process the government prints money to lend to itself, adding to the overall money supply in the process.

In recent times, thanks to an utterly insane program spearheaded by Greenspan's successor, Ben Bernanke, called quantitative easing, the Fed has gotten into the habit of buying more than just T-bills and is printing billions of dollars every week to buy private assets like mortgages. In practice, however, the Fed's main tool for regulating the money supply during the Greenspan years wasn't its purchase of securities or control over margin requirements, but its manipulation of interest rates.

Here's how this works: When a bank falls short of the cash it needs to meet its reserve requirement, it can borrow cash either from the Fed or from the reserve accounts of other banks. The interest rate that bank has to pay to borrow that money is called the *federal funds rate*, and the Fed can manipulate it. When rates go up, borrowers are discouraged from taking out loans, and banks end up rolling back their lending. But when the Fed cuts the funds rate, banks are suddenly easily able to borrow the cash they need to meet their reserve requirements, which in turn dramatically impacts the amount of new loans they can issue, vastly increasing the money in the system.

The upshot of all of this is that the Fed has enormous power to create money both by injecting it directly into the system and by allowing private banks to create their own new loans. If you have a productive economy and an efficient financial services industry that rapidly mar-

> Because we at the Federal Reserve were concerned about sharp reactions in the markets that **had grown accustomed to an unsustainable combination of high returns and low volatility** [emphasis mine], we chose a cautious approach . . . We recognized . . . that our shift could impart uncertainty to markets, and many of us were concerned that a large immediate move in rates could create too big a dose of uncertainty, which could destabilize the financial system.

Translation: everybody was used to making unrealistic returns, and we didn't want to spoil the party by instituting a big rate hike. (Cue Claude Rains in *Casablanca* after the Nazis shut down Rick's roulette game: "But everybody's having such a good time!") Instead, Greenspan's response to the growing bubble in the summer of 1994 was a very modest hike of one-half of one percentage point.

Now here comes the crazy part. At around the same time that Greenspan was testifying before the Senate that a cautious approach was fine, that no drastic action was needed, and there was no danger out there of a bubble, he was saying virtually the exact opposite at a meeting of the Federal Open Market Committee (FOMC), the humorously secretive and Politburo-esque body charged with making rate adjustments. Here is Greenspan on May 17, 1994:

> I think there's still a lot of bubble around; we have not completely eliminated it. Nonetheless, we have the capability, I would say at this stage, to move more strongly than we usually do without cracking the system.

This testimony is amazing in retrospect because about eight years later, after the crash of the tech bubble, Greenspan would openly argue that bubbles are impossible to see until they pop. It is, he would say in 2002, "very difficult to definitively identify a bubble until after the fact—that is, when its bursting confirmed its existence."

A few months after Greenspan warned the FOMC that there was still some "bubble around," he suddenly announced that the bubble had been popped. At an FOMC meeting in August 1994, he said that the May rate hike of one-half a percentage point had solved the problem. "With the May move," he said, "I think we demonstrated that the bubble for all practical purposes had been defused."

About a half year later, in February 1995, Greenspan would raise rates for the last time for many years. "One can say that while the stock market is not low, it clearly is not anywhere close to being as elevated as it was a year or so ago," he said.

Within a few months after that, by July 1995, Greenspan was back to *cutting* rates, slashing the funds rate from 6 percent to 5.75 percent, flooding the economy with money at a time when the stock market was exploding. With easy credit everywhere and returns on savings and CDs at rock bottom, everyone and his brother rushed ass first into the tech-fueled stock market. "That's the beginning of the biggest stock market bubble in U.S. history," says Fleckenstein.

But Greenspan's biggest contribution to the bubble economy was psychological. As Fed chief he had enormous influence over the direction of the economy and could have dramatically altered history simply by stating out loud that the stock market was overvalued.

And in fact, Greenspan in somewhat hesitating fashion tried this—with his famous December 1996 warning that perhaps "irrational exuberance" had overinflated asset values. This was spoken in the full heat of the tech bubble and is a rare example of Greenspan speaking, out loud, the impolitic truth.

It's worth noting, however, that even as he warned that the stock market was overheated, he was promising to not do a thing about it. On the same day that he spoke about "irrational exuberance," Greenspan said that the Fed would only act if "a collapsing financial asset bubble does not threaten to impair the real economy." Since popping a bubble *always* impairs the real economy, Greenspan was promising never to do anything about anything.

Despite Greenspan's rather explicit promise to sit on his liver-spotted hands during the bubble, Wall Street reacted with unbridled horror at Greenspan's "irrational exuberance" quote, which made sense: the Internet stock party was just getting going and nobody wanted to see it end. A mini-panic ensued as the Street brutally responded to Greenspan's rhetoric, with the NYSE plunging 140 points in the first hour of trading the day after his comments. The *New York Times* even ran a front-page story with the headline "Stocks Worldwide Dive as Greenspan Questions Euphoria."

For a man who hated to be disliked on Wall Street, the reaction was a nightmare. "Greenspan was freaked out by the response," says one newspaper reporter who covered Greenspan on a daily basis at the time. "That [irrational exuberance business] was the one time he said something in a way that was clear enough and quotable enough to make the newspapers, and all hell broke loose."

And so, true to his psychological pattern, Greenspan spent much of the next four years recoiling from his own warning, turning himself all the way around to become head cheerleader to the madness.

In fact, far from expressing concern about "irrational" stock values, Greenspan subsequently twisted himself into knots finding new ways to make sense of the insane share prices of the wave of Worthless.com stocks that were flooding the market at the end of that decade. The same man who as early as 1994 was warning the FOMC about "a lot of bubble around" took to arguing that there *was* no bubble.

Greenspan's eventual explanation for the growing gap between stock prices and actual productivity was that, fortuitously, the laws of nature had changed—humanity had reached a happy stage of history where bullshit could be used as rocket fuel. In January 2000 Greenspan unveiled a theory, which he would repeat over and over again, that the economy had entered a new era, one in which all the rules were being rewritten:

> When we look back at the 1990s, from the perspective of say 2010, the nature of the forces currently in train will have presumably become clearer. We may conceivably conclude from that vantage point that, at the turn of the millennium, the American economy was experiencing a once-in-a-century acceleration of innovation, which propelled forward productivity . . . at a pace not seen in generations, if ever.

In a horrifyingly literal sense, Greenspan put his money where his mouth was, voting for the mania with the Fed's money. An example: On November 13, 1998, a company called theglobe.com went public, opening at $9 and quickly jumping to $63.50 at the close of the first day's trading. At one point during that day, the stock market briefly valued the shares in theglobe.com at over $5 billion—this despite the fact that the company's total earnings for the first three quarters of that year were less than $2.7 *million.*

Four days after that record-shattering IPO, which clearly demonstrated the rabid insanity of the tech-stock tulipomania, Alan Greenspan again doused the market with lighter fluid, chopping rates once more, to 4.75 percent. This was characteristic of his behavior throughout the boom. In fact, from February 1996 through October 1999, Greenspan expanded the money supply by about $1.6 trillion, or roughly 20 percent of GDP.

Even now, with the memory of the housing bubble so fresh, it's hard to put in perspective the craziness of the late-nineties stock market. Fleckenstein points out that tech stocks were routinely leaping by 100 percent of their value or more on the first day of their IPOs, and cites Cobalt Networks (482 percent), Foundry Networks (525 percent), and Akamai Technologies (458 percent) as examples. All three of those companies traded at one hundred times sales—meaning that if you bought the entire business and the sales generated incurred no expenses, it would have taken you one hundred years to get your money back.

According to Greenspan, however, these companies were not necessarily valued incorrectly. All that was needed to make this make sense was to rethink one's conception of "value." As he put it during the boom:

> [There is] an ever increasing conceptualization of our Gross Domestic Product—the substitution, in effect, of ideas for physical value.

What Greenspan was saying, in other words, was that there was absolutely nothing wrong with bidding up to $100 million in share value some hot-air Internet stock, because the lack of that company's "physical value" (i.e., the actual money those three employees weren't earning) could be overcome by the inherent value of their "ideas."

To say that this was a radical reinterpretation of the entire science of economics is an understatement—economists had never dared measure "value" except in terms of actual concrete production. It was equivalent to a chemist saying that concrete becomes gold when you paint it yellow. It was lunacy.

Greenspan's endorsement of the "new era" paradigm encouraged all the economic craziness of the tech bubble. This was a pattern he fell into repeatedly. When a snooty hedge fund full of self-proclaimed geniuses called Long-Term Capital Management exploded in 1998, thanks to its managers' wildly irresponsible decision to leverage themselves one hundred or two hundred times over or more to gamble on risky derivative bets, Greenspan responded by orchestrating a bailout, citing "systemic risk" if the fund was allowed to fail. The notion that the Fed would intervene to save a high-risk gambling scheme like LTCM was revolutionary. "Here, you're basically bailing out a hedge fund," says Dr. John Makin, a former Treasury and Congressional Budget Office official. "This was a bad message to send. It basically said to people, take more risk. Nobody is going to stop you."

When the Russian ruble collapsed around the same time, causing massive losses in emerging markets where investors had foolishly committed giant sums to fledgling economies that were years from real productivity, Greenspan was spooked enough that he announced a surprise rate cut, again bailing out dumb investors by letting them borrow their way out of their mistakes. "That's what capitalism is supposed to be about—creative destruction," says Fleckenstein. "People who take too much risk are supposed to fail sometimes." But instead of letting nature take its course, Greenspan came to the rescue every time some juiced-up band of Wall Street greedheads drove their portfolios into a tree.

Greenspan was even dumb enough to take the Y2K scare seriously, flooding the markets with money in anticipation of a systemwide computer malfunction that, of course, never materialized. We can calculate how much money Greenspan dumped into the economy in advance of Y2K; between September 20 and November 10, 1999, the Fed printed about $147 billion extra and pumped it into the economy. "The crucial issue . . . is to recognize that we have a Y2K problem," he said at the century's final FOMC meeting. "It is a problem about which we don't want to become complacent."

Again, all of these rate cuts and injections—in response to LTCM, the emerging markets crash, and Y2K—were undertaken in the middle of a raging stock market bubble, making his crisis strategy somewhat like trying to put out a forest fire with napalm.

By the turn of the century, the effect of Greenspan's constant money printing was definite and contagious, as it was now widely understood that every fuckup would be bailed out by rivers of cheap cash. This was where the term "Greenspan put" first began to be used widely.

Aside: a "put" is a financial contract between two parties that gives the buyer the option to sell a stock at a certain share price. Let's say IBM is trading at 100 today, and you buy 100 puts from Madonna at 95. Now imagine the share price falls to 90 over the course of the next two weeks. You can now go out and buy 100 shares at 90 for $9,000, and then exercise your puts, obligating Madonna to buy them back at 95, for $9,500. You've then earned $500 betting against IBM.

The "Greenspan put" referred to Wall Street's view of cheap money from the Fed playing the same hedging role as a put option; it's a kind of insurance policy against a declining market you keep in your back pocket. Instead of saying, "Well, if IBM drops below ninety-five, I can always sell my put options," Wall Street was saying, "Well, if the market drops too low, Greenspan will step in and lend us shitloads of money." A Cleveland Fed official named Jerry Jordan even expressed the idea with somewhat seditious clarity in 1998:

> I have seen—probably everybody has now seen—newsletters, advisory letters, talking heads at CNBC, and so on saying there is no risk that the stock market is going to go down because even if it started down, the Fed would ease policy to prop it back up.

Eventually, the Iowa professor Paul Weller, along with University of Warwick professors Marcus Miller and Lei Zhang, would formally identify this concept in a paper called "Moral Hazard and the U.S. Stock Market: Analyzing the 'Greenspan Put.' " By then, however, the term "Greenspan put" had been around for years, and the very fact that it was now being formally studied is evidence of the profound effect it had on the markets.

"Investors came to believe in something the Fed couldn't really deliver," says Weller now. "There was this belief that the Fed would always provide a floor to the market."

"His effect on the psychology is the most important thing you have to look at," says the manager of one well-known hedge fund. "There was this belief that Greenspan would always be the lender of last resort, that we would always have the government bail us out."

"It was all psychological. If people just *thought* Greenspan was in charge, things would be okay," says Wesbury. "Even John McCain said that if Greenspan were ever to die, he would just prop him up in the corner and put sunglasses on him, like in *Weekend at Bernie's*.* The belief that he would be there is the thing."

"It's a two-pronged problem," says Fleckenstein. "Number one, he's putting in this rocket fuel to propel the speculation. And number two, he's giving you the confidence that he's going to come in and save the day . . . that the Fed will come in and clean up the mess."

The idea that Greenspan not even covertly but overtly encouraged irresponsible speculation to a monstrous degree is no longer terribly controversial in the financial world. But what isn't discussed all that often is how Greenspan's constant interventions on behalf of Wall Street speculators dovetailed with his behavior as a politician and as a regulator during the same period.

Even as Greenspan was using the vast power of the state to bail out the very assholes who were selling back-of-the-napkin Internet startups to pension funds or betting billions in borrowed cash on gibberish foreign exchange derivative trades, he was also working round the clock, with true Randian zeal, to destroy the government's regulatory infrastructure.

As chief overseer of all banking activity the Fed was ostensibly the top cop on the financial block, but during his years as Fed chief Greenspan continually chipped away—actually it was more like hacking away, with an ax—at his own regulatory authority, diluting the Fed's power to enforce margin requirements, restrict derivative trades, or prevent unlawful

*"I would not only reappoint Mr. Greenspan; if Mr. Greenspan should happen to die, God forbid . . . I would prop him up and put a pair of dark glasses on him."—then–presidential candidate John McCain, 2000.

mergers. What he was after was a sort of cynical perversion of the already perverse Randian ideal. He wanted a government that was utterly powerless to interfere in the workings of private business, leaving just one tool in its toolbox—the ability to funnel giant sums of money to the banks. He turned the Fed into a Santa Claus who was legally barred from distributing lumps of coal to naughty kids.

Greenspan's reigning achievement in this area was his shrewd undermining of the Glass-Steagall Act, a Depression-era law that barred insurance companies, investment banks, and commercial banks from merging. In 1998, the law was put to the test when then–Citibank chairman Sandy Weill orchestrated the merger of his bank with Travelers Insurance and the investment banking giant Salomon Smith Barney.

The merger was frankly and openly illegal, precisely the sort of thing that Glass-Steagall had been designed to prevent—the dangerous concentration of capital in the hands of a single megacompany, creating potential conflicts of interest in which insurers and investment banks might be pressed to promote stocks or policies that benefit banks, not customers. Moreover, Glass-Steagall had helped prevent exactly the sort of situation we found ourselves subject to in 2008, when a handful of companies that were "too big to fail" went belly up thanks to their own arrogance and stupidity, and the government was left with no choice but to bail them out.

But Weill was determined to do this deal, and he had the backing of Bill Clinton, Clinton's Treasury secretary Bob Rubin (who would go on to earn $100-plus million at postmerger Citigroup), and, crucially, Alan Greenspan. Weill met with Greenspan early in the process and received what Weill called a "positive response" to the proposal; when the merger was finally completed, Greenspan boldly approved the illegal deal, using an obscure provision in the Bank Holding Company Act that allowed the merger to go through temporarily. Under the arrangement, the newly created Citigroup would have two years to divest itself of its illegal insurance company holdings, plus three additional years if Greenspan approved a series of one-year grace periods. That gave all the parties involved time to pass a new law in Congress called the Gramm-Leach-Bliley Act, which would legalize the deal post factum.

It was a move straight out of *Blazing Saddles:* Greenspan basically had this newly formed megafirm put a gun to its own head and pull the "One move and the nigger gets it!" routine before Congress.

Greenspan himself put it in even starker terms, not so subtly threatening that if Congress failed to play ball, the state would be forced to pay for a wave of insurance and banking failures. "Without congressional action to update our laws," he said in February 1999, "the market will force ad hoc administrative responses that lead to inefficiencies and inconsistencies, expansion of the federal safety net, and potentially increased risk exposure to the federal deposit insurance funds."

Congress had fought off pressure to repeal Glass-Steagall numerous times in the eighties and early nineties, but this time, in the face of Greenspan's threats and this massive deal that had already been end-run into existence, it blinked. Gramm-Leach-Bliley thus became law, a move that would lead directly to the disasters of 2008.

And once he was finished with Glass-Steagall, Greenspan took aim at the derivatives market, where a rogue government official named Brooksley Born had committed the cardinal sin of suggesting that derivatives, like foreign exchange swaps and credit default swaps, posed a potential danger to the economy and might be necessary to regulate. Born, at the time the head of the Commodity Futures Trading Commission, which has purview over derivatives, had in the spring of 1998 issued something called a *concept release,* sort of the government bureaucracy version of a white paper, calling for suggestions on potential regulation of the over-the-counter derivatives market. The twenty-odd-page paper detailed many of the potential risks of derivative trading and today looks a lot like a Nostradamus testament, so accurately does it predict derivative-fueled disasters like the collapse of AIG.

When a draft of Born's concept release began circulating on the Hill in March and April of that year, Bill Clinton's inner circle on economic matters—including former Goldman chief and then–Treasury secretary Bob Rubin, his deputy Gary Gensler, Greenspan at the Fed, and then–SEC chief Arthur Levitt—all freaked out. This was despite the fact that Born hadn't even concretely proposed any sort of regulation yet—she was just trying to initiate a discussion about the *possibility* of regulation. Nonetheless, a furor ensued, and at a critical April 21, 1998, meeting of

the President's Working Group on Financial Markets—a group that includes primarily the heads of the Treasury (at the time, Rubin), the SEC (Levitt), the CFTC (Born), and the Fed (Greenspan)—the other members openly pressured Born to retrench.

"It was a great big conference table in this ornate room that the secretary of the Treasury had," says Michael Greenberger, who at the time worked under Born as the head of the CFTC's Division of Trading and Markets. "Not only were the four principals there, but everybody in the government who has any regulatory responsibility for financial affairs was there—the comptroller of the currency, the chairman of the FDIC, the Office of Thrift Supervision, the White House adviser, the OMB, the room was packed with people.

"And if you were a staff member, you sat behind your principal," he goes on. "My seat was directly behind Brooksley and Greenspan. I could have reached out and touched either one of them. And Greenspan turned to her, and his face was red, and he wasn't hollering, but he was quite insistent that she was making a terrible mistake and that she should stop."

Born had complete legal authority to issue her concept release without interference from the Working Group, the president, or anyone else—in fact, the seemingly overt effort to interfere with her jurisdiction was "a violation, maybe even rising to the level of a criminal violation," according to Greenberger. Despite these legally questionable efforts of Rubin and Greenspan, Born did eventually release her paper on May 7 of that year, but to no avail; Greenspan et al. eventually succeeded not only in unseating Born from the CFTC the next year, but in passing a monstrosity called the Commodity Futures Modernization Act of 2000, which affirmatively deregulated the derivatives market.

The new law, which Greenspan pushed aggressively, not only prevented the federal government from regulating instruments like collateralized debt obligations and credit default swaps, it even prevented the states from regulating them using gaming laws—which otherwise might easily have applied, since so many of these new financial wagers were indistinguishable from racetrack bets.

The amazing thing about the CFMA was that it was passed immediately after the Long-Term Capital Management disaster, a potent and obvious example of the destructive potential inherent in an unregulated derivatives market. LTCM was a secretive hedge fund that was making huge bets without collateral and keeping massive amounts of debt off its balance sheet, à la Enron—the financial equivalent of performing open heart surgery with unwashed hands, using a Super 8 motel bedspread as an operating surface.

None of this fazed Greenspan, who apparently never understood what derivatives are or how they work. He saw derivatives like credit default swaps—insurance-like contracts that allow a lender to buy "protection" from a third party in the event his debtor defaults—as brilliant innovations that not only weren't risky, but reduced risk.

"Greenspan saw credit derivatives as a device that enhanced a risk-free economic environment," says Greenberger. "And the theory was as follows: he's looking at credit derivatives, and he's saying everyone is going to have insurance against breakdowns . . . But what he didn't understand was that the insurance wasn't going to be capitalized."

In other words, credit default swaps and the like allowed companies to sell something like insurance protection without actually having the money to pay that insurance—a situation that allowed lenders to feel that they were covered and free to take more risks, when in fact they were not. These instruments were most often risk enhancers, not risk eliminators.

"It wasn't like buying insurance, car insurance, life insurance, something else, where it's regulated and the companies have to be capitalized," Greenberger goes on. "These guys were selling insurance without being capitalized." AIG, which imploded in 2008 after selling nearly a half billion dollars' worth of insurance despite having practically no money to pay off those bets, would end up being the poster child for that sort of risk.

But this problem should have been obvious way before AIG, particularly to someone in Greenspan's position. In fact, even by 1998, by the time LTCM was over, the country had already experienced numerous derivatives-based calamities: the 1987 crash, the Orange County bankruptcy of 1994, the Bankers Trust scandal of 1995, and LTCM. Nonetheless, Greenspan refused to see the danger. In March 1999, just months after he himself had orchestrated a bailout for LTCM, he said

that "derivatives are an increasingly important vehicle for unbundling risk." He then said he was troubled that the "periodic emergence of financial panics" had inspired some to consider giving regulators more power to monitor derivative risk, instead of leaving the banks to monitor risk on their own.

An example of the kind of private "monitoring" that Greenspan championed was Long-Term Capital Management's risk models. According to the fund's initial calculations, it would lose 50 percent of its portfolio only once every 10^{30} days, i.e., one would have to sit and wait for several billion times the life of the universe for such a disaster to happen. The fund would actually lose pretty much its entire portfolio just a few years into its existence.

Nonetheless, Greenspan just months after this collapse said that regulators' risk models were "much less accurate than banks' risk measurement models." This was the line he sold to Congress before it passed the CFMA; he also insisted that the derivatives market needed exemptions from regulation in order to remain competitive internationally. But he made clear his real reasons for pushing derivatives deregulation in a speech to the Futures Industry Association in March 1999:

> It should come as no surprise that the profitability of derivative products . . . is a factor in the significant gain of the overall finance industry's share of American corporate output during the past decade. In short, the value added of derivatives themselves derives from their ability to enhance the process of wealth creation.

Translating that into English: I recognize that derivatives are making everyone shitloads of money, so I'll leave them alone.

It was in the immediate wake of all these historically disastrous moves—printing 1.7 trillion new dollars in the middle of a massive stock bubble, dismantling the Glass-Steagall Act, deregulating the derivatives market, blowing off his regulatory authority in the middle of an era of rampant fraud—that Greenspan was upheld by the mainstream financial and political press as a hero of almost Caesarian stature. In February 1999, *Time* magazine even put him on the cover, flanked by

Clinton officials Bob Rubin and Larry Summers, next to the preposterous headline "The Committee to Save the World: The inside story of how the Three Marketeers have prevented a global economic meltdown—so far."

That these guys were actually *anti*-Marketeers who had not prevented but *caused* an economic meltdown was an irony that even in retrospect was apparently lost on *Time,* which would make the exact same idiotic mistake in 2009, when it made Greenspan's similarly bubble-manic successor, Ben Bernanke, its Person of the Year. In any case, the 1999 *Time* cover captured Greenspan at his peak; he had used the Fed's power to turn himself into the great indispensable superhero of the investor class, worshipped on the one hand for the uncompromising free-market orthodoxy of his crotchety public statements, and giddily prized on the other hand for his under-the-table subsidies of the nation's bankers.

But even as Greenspan sheltered Wall Street from changes in the weather, when it came to using the Fed's powers to rein in abuses he proclaimed helplessness before the forces of the free market. The same person who intervened to counteract the market's reaction to the implosion of Long-Term Capital Management and the Russian ruble even had the balls to tell Congress that he, Alan Greenspan, did not have the right to question the wisdom of the market, when for instance the market chose to say that a two-slackers-in-a-cubicle operation like theglobe.com was worth $500 billion.

"To spot a bubble in advance," he told Congress in 1999, "requires a judgment that hundreds of thousands of informed investors have it all wrong." He added, with a completely straight face, "Betting against markets is usually precarious at best."

Some said he was just naïve, or merely incompetent, but in the end, Greenspan was most likely just lying. He castrated the government as a regulatory authority, then transformed himself into the Pablo Escobar of high finance, unleashing a steady river of cheap weight into the crack house that Wall Street was rapidly becoming.

Greenspan's response to the horrific collapse of the tech bubble in 2000–2001 was characteristic and predictable. More than $5 trillion worth of wealth had been destroyed in worthless tech stocks, but instead of letting investors feel the pain they deserved, Greenspan did what he had always done: he flooded the market with money all over again and inflated a new bubble. Only this was the biggest "Greenspan put" of all: in the wake of the tech bubble he cut rates eleven consecutive times, all the way down to 1 percent, an all-time low, and began talking out loud about housing and mortgages as the new hot table in the casino.

"When the real estate bubble came along as a consequence of the money printing that was used to sort of drink ourselves sober after the equity bubble, I knew it was going to be an even bigger disaster," says Fleckenstein.

Looking back now at the early years in the 2000s, Greenspan's comments almost seem like the ravings of a madman. The nation's top financial official began openly encouraging citizens to use the equity in their homes as an ATM. "Low rates have also encouraged households to take on larger mortgages when refinancing their homes," he said. "Drawing on home equity in this manner is a significant source of funding for consumption and home modernization."

But he went really crazy in 2004, when he told America that adjustable-rate mortgages were a good product and safer, fixed-rate mortgages were unattractive. He said the following in a speech to the Credit Union National Association Governmental Affairs Conference in February 2004:

> Indeed, recent research within the Federal Reserve suggests that many homeowners might have saved tens of thousands of dollars had they held adjustable-rate mortgages rather than fixed-rate mortgages during the past decade, though this would not have been the case, of course, had interest rates trended sharply upward . . .
>
> American consumers might benefit if lenders provided greater mortgage product alternatives to the traditional fixed-rate mortgage. To the degree that households are driven by fears of payment

shocks but are willing to manage their own interest rate risks, the traditional fixed-rate mortgage may be an expensive method of financing a home.

The most revolting thing about Greenspan's decision to wave a flag for adjustable-rate mortgages was the timing.

Greenspan was nearing the end of his reign as Fed chief. He would be renominated one more time by George W. Bush, but his last term would end in January 2006.

So the timing of that speech to the Credit Union National Association Conference in February 2004 is remarkable. He had been cutting rates or holding them flat for years. The economy at the time was full of easy money and people everywhere were borrowing fortunes and buying beyond their means. Greenspan himself knew he was on his way out soon, but he also knew one other thing: he was about to start raising interest rates.

In fact, in June 2004, just a few months after he encouraged Americans to shun fixed-rate mortgages for adjustable-rate mortgages, Greenspan raised rates for what would be the first of seventeen consecutive times. He would raise rates at every FOMC meeting between June 2004 and the time he left office two years later, more than quadrupling interest rates, moving them from 1 percent to 4.5 percent. In other words, he first herded people into these risky mortgage deals and then, seemingly as a gift to the banks on his way out of town, spent two straight years jacking up rates to fatten the payments homeowners had to make to their lenders.

"He made that argument [about adjustable-rate mortgages] right before he started raising interest rates. Are you kidding me?" said one hedge fund manager. "All he was doing was screwing the American consumer to help the banks . . . If you had had people on thirty-year fixed mortgages, you wouldn't have had half these houses blowing up, because mortgages would have remained steady. Instead . . . it was the most disingenuous comment I've ever heard from a government official."

Greenspan's frantic deregulation of the financial markets in the late nineties had led directly to the housing bubble; in particular, the deregulation of the derivatives market had allowed Wall Street to create a vast infrastructure for chopping up mortgage debt, disguising bad loans as AAA-rated investments, and selling the whole mess off on a secondary market as securities. Once Wall Street perfected this mechanism, it was suddenly able to create hundreds of billions of dollars in crap mortgages and sell them off to unsuspecting pension funds, insurance companies, unions, and other suckers as grade-A investments, as I'll detail in the next chapter.

The amount of new lending was mind-boggling: between 2003 and 2005, outstanding mortgage debt in America grew by $3.7 trillion, which was roughly equal to the entire value of all American real estate in the year 1990 ($3.8 trillion). In other words, Americans in just two years had borrowed the equivalent of two hundred years' worth of savings.

Any sane person would have looked at these numbers and concluded that something was terribly wrong (and some, like Greenspan's predecessor Paul Volcker, did exactly that, sounding dire warnings about all that debt), but Greenspan refused to admit there was a problem. Instead, incredibly, he dusted off the same old "new era" excuse, claiming that advances in technology and financial innovation had allowed Wall Street to rewrite the laws of nature again:

> Technological advances have resulted in increased efficiency and scale within the financial services industry . . . With these advances in technology, lenders have taken advantage of credit-scoring models and other techniques for efficiently extending credit to a broader spectrum of consumers.

The kinds of technological advances Greenspan was talking about were actually fraud schemes. In one sense he was right: prior to the 2000s, the technology did not exist to make a jobless immigrant with no documentation and no savings into an AAA-rated mortgage risk. But now, thanks to "technological advances," it was suddenly possible to lend trillions of dollars to millions of previously unsuitable borrowers! This was Greenspan's explanation for the seemingly inexplicable surge in new home buying.

The results of all these policies would be catastrophic, of course, as the collapse of the real estate market in 2007–8 would wipe out roughly 40 percent of the world's wealth, while Greenspan's frantic printing of trillions of new dollars after the collapse of the tech boom would critically devalue the dollar. In fact, from 2001 to 2006, the dollar would lose 24 percent of its value versus the foreign currencies in the dollar index and 28 percent of its value versus the Canadian dollar. Even tinpot third world currencies like the ruble and the peso gained against the dollar during this time. And yet Greenspan insisted at the end of this period that the devaluation of the dollar was not really a problem—so long as you didn't travel abroad!

> So long as the dollar weakness does not create inflation . . . then I think it's a market phenomenon, which aside from those who travel the world, has no real fundamental consequences.

No real fundamental consequences? For Greenspan to say such a thing proved he was either utterly insane or completely dishonest, since even the world's most stoned college student understands that a weak dollar radically affects real wealth across the board: we buy foreign oil in dollars, and since energy costs affect the price of just about everything, being able to buy less and less oil with a dollar as time goes on makes the whole country that much poorer. It's hard to overstate how utterly mad it is for a Fed chairman in the age of the global economy to claim that a weak currency only affects *tourists.* It's a little bit like saying a forest fire only really sucks if you're a woodpecker.

In any case, by the time Greenspan left the Fed in 2006, Americans had lost trillions upon trillions of dollars in two gigantic bubble scams, and we had gone from being a nation with incredible stored wealth in personal savings to being a country that collectively is now way over its head in hock, with no way out in sight. As of this writing, America's international debt is somewhere in the region of $115 trillion, with our debt now well over 50 percent of GDP. This is debt on a level never before seen in a modern industrialized country.

It sounds facile to pin this all on one guy, but Greenspan was the crucial enabler of the bad ideas and greed of others. He blew up one bubble and then, when the first one burst, he printed money to inflate

the next one. That was the difference between the tech and the housing disasters. In the tech bubble, America lost its own savings. In the housing bubble, we borrowed the shirts we ended up losing, leaving us in a hole twice as deep.

It's important to note that throughout this entire time, while Greenspan was printing trillions of dollars and manipulating the economy to an elaborate degree, he was almost completely unaccountable to voters. Except for the right of an elected president to nominate the Fed chief, voters have no real say over what the Fed does. Citizens do not even get to see transcripts of FOMC meetings in real time; we're only now finding out what Greenspan was saying during the nineties. And despite repeated attempts to pry open the Fed's books, Congress as of this writing has been unsuccessful in doing so and still has no idea how much money the Fed has lent out at the discount window and to whom.

Congress's authority over the Fed is so slight that when Los Angeles congressman Brad Sherman passed an amendment capping the amount of emergency assistance to banks the Fed could loan out at a still-monstrous $4 trillion, it was considered a big victory.

"We were lucky to get that," Sherman says.

Really the only time the public could even get an audience with Greenspan was through his compulsory appearances before Congress, which Greenspan plainly loathed and for which he set strict time limits. Texas congressman Ron Paul explains that Greenspan was so tight with his time that members of Congress would have to wait in line for months just to get this or that question before His Highness in committee hearings.

"He might come at ten a.m. and say his limit was one or two [congressmen]," Paul says now. "So if you were at the bottom of the list, you wouldn't get a chance to ask the question."

As a result, Paul says, members who didn't get questions in would have to wait months until their next shot. "If you didn't get to ask your question, you'd be high on the list the next time," he says. "That was the best you could hope for."

All of which makes Greenspan's exit from power that much harder to swallow. He was unrepentant almost to the bitter end. Even as late as

November 2007, with the international financial community already beginning to erupt in panic thanks to the latest bubble explosion, Greenspan shrugged. "I have no particular regrets," he told audiences in Norway. "The housing bubble is not a reflection of what we did."

It wasn't until October 2008, after the collapses of Bear Stearns and Lehman Brothers and AIG, after massive federal bailouts were implemented to stave off total panic, that Greenspan budged—sort of. In testimony before Henry Waxman's Committee on Oversight and Government Reform, he admitted, sort of, that his Randian faith in the eternal efficacy of self-regulating markets had been off, a little.

"I've found a flaw," he told Waxman. "I don't know how significant or permanent it is. But I've been very distressed by that fact."

Waxman at that instant found himself in an unusual position, representing a whole generation of infuriated Greenspan critics and opponents who had never gotten the Maestro to apologize for a damn thing. It would have been understandable had he been overwhelmed by the pressure of the moment. Instead Waxman calmly pressed Greenspan.

"Were you wrong?"

Greenspan's answer to this question was priceless—a landmark moment in the annals of political narcissism, the Bobby Thomson walk-off homer of unrepentant dickdom. Was he wrong?

"Partially," Greenspan answered.

That moment is what passes for a major victory for American democracy these days—an elected official getting at least one semi-straight answer out of an unaccountable financial bureaucrat.

But that's about as good as it gets. In reality, even if Greenspan got taken down a fraction of an inch toward the end of his life, his belief system—or what passes for his belief system—remains ascendant, if not dominant, in the international finance culture. He raised a generation of Wall Street bankers who under his tutelage molded themselves in the image of Randian supermen, pursuing the mantra of personal profit with pure religious zeal.

In fact, what made the bubbles possible was that the people who ran banks like Goldman Sachs and Morgan Stanley and Citigroup during the Greenspan era were possessed by this cultist fervor, making them genuinely blind to the destructive social consequences of their actions and infuriatingly immune to self-doubt. The Randian mindset was so widespread in the finance world that even after the horrific 2008 crash, executives from Goldman Sachs could be seen insisting in public that Jesus himself would have approved of their devotion to personal profit ("The injunction of Jesus to love others as ourselves is an endorsement of self-interest," Goldman international adviser Brian Griffiths told parishioners of London's St. Paul's Cathedral). That sort of moral blindness turbocharged the greed on the private banking side, but it was Greenspan's cynical construction of a vast and unaccountable welfare state that made the theft scheme virtually unstoppable.

The important thing to remember about the Alan Greenspan era is that despite all the numbers and the inside-baseball jargon about rates and loans and forecasts, his is not a story about economics. The Greenspan era instead is a crime story. Like drug dealing and gambling and Ponzi schemes, bubbles of the sort he oversaw are rigged games with preordained losers and inherently corrupting psychological consequences. You play, you get beat, in more ways than one.

Greenspan staked the scam, printing trillions upon trillions of dollars to goad Americans into playing a series of games they were doomed from the start to lose to the dealer. In the end the printed wealth all disappeared and only the debts remained. He probably did this just because he wanted to see his face on magazine covers and be popular at certain Upper East Side cocktail parties. His private hang-ups in this way shaped the entire scam of modern American politics: a pure free market for the suckers, golden parachutes for the Atlases.

4

Blowout

The Commodities Bubble

In the summer of 2008, Priscilla Carillo, a twenty-four-year-old living near San Bernardino, had some rough luck. She had been working as a temp at a warehouse and also going to school at Chaffey Community College, about forty minutes away from where she was living at the time. She was humping it back and forth in a beat-up Nissan Altima, making a go of it. She says her mom, thinking she was being helpful, had booted her out of the house when she turned eighteen, told her to make her own way. You know, the American way.

"I always thought Latinos lived with their parents until they were forty," she says now. "I guess I was different."

Then, at the beginning of 2008, Priscilla started to notice a problem. Gas prices were going up—*way* up. They were steaming past four dollars a gallon. Since the trip to her community college was a long one, it soon became unaffordable. She dumped school and went to work full-time. But then her temp agency went under and she lost her job. Now Priscilla was broke and unable to pay rent. In June and July 2008, she was living in her car.

"I'd park at a library or in a park or something," she says now. "I didn't know I couldn't sleep in residential neighborhoods at night. I got picked up by the cops a bunch of times. They thought I was a prostitute. I told them, man, I'm just sleeping."

Halfway across the country, at almost exactly the same time, a businessman named Robert Lukens was starting to feel a squeeze. He ran a contracting firm called Lukens Construction in Reading, Pennsylvania. Lukens had seven employees and his business had been in his family for three generations, founded by his father close to forty years back.

He hadn't wanted to get into the family business, but circumstances made that decision for him. Way back in 1981 he'd moved to Richmond, Virginia, and in the space of a week had gotten married and then was laid off by Ryan Homes, one of the biggest contracting companies in America.

Now, with a new wife and no job, he reluctantly went back to work for his father, who had taken over Lukens Construction from his own father and with whom he had a difficult relationship. But father and son smoothed it out, stuck it out, and made it work. Some fourteen years later, in 1995, Robert Lukens took over the business himself, and in describing the firm he sounded like a man deeply proud of his family's business. "We do high-end contracting, really nice work," he says. Not cookie-cutter houses, he says, but custom additions and "lots of word-of-mouth referrals." Heading into 2008, Lukens says, he was doing fine.

"But then all of a sudden I started having high energy costs," he says. "Used to be I'd pay five hundred, six hundred dollars a week for gas. Now, in July of 2008, I'm suddenly paying twelve hundred dollars a week for gas. And not only that—all my vendors are suddenly hitting me with fuel costs. Used to be if I got a delivery of lumber, the delivery would be figured into the price. Now they'd hit me with a surcharge—a hundred and twenty-five bucks for the delivery or whatever. Lumber. Concrete. Stuff like that."

About the same time that Lukens was seeing those price hikes, a biology student with dreams of becoming a doctor named Sam Sereda was heading home for the summer. Sereda was doing his undergrad at Gordon College on the North Shore of Massachusetts, but his home was in Sunnyvale, in the Bay Area out in California. Sereda was doing everything right in his young life. His grades were good, he was making money in his spare time by tutoring kids from Hamilton Wenham High in AP Bio. For the summer he had an internship set up with a Bay Area company called Genentech in San Francisco, and was planning on taking an advanced calc class at West Valley College in Saratoga, to pick up a few extra credits for his upcoming senior year.

"But then gas prices, they went from like three bucks to over four bucks a gallon," he says now. "My family was going through some financial problems at the time, too. I ended up having to cancel the internship. The forty-minute drive was too long, it cost me too much money."

The calc class went out the window, too. "Couldn't afford that drive either," he says now. "I ended up having to do twenty credits in one semester when I got back to Massachusetts. I know how this sounds, but with gas prices the way they were . . . my only real option for that summer was to sit in the house and do nothing. My brother was ill at the time—my family and I made the decision, the best thing for me was just to stay home."

And while all of this was going on, a woman named Diane Zollinger was gainfully employed, no serious economic worries on the horizon. Her problem was that she lived in Montana. In Montana, everything is far from everything else. She had a good job in Bozeman, but Bozeman was thirty-five miles from her home in Livingston. She was driving seventy miles a day to work when the price of gas shot up to $4.85 a gallon. Her car got twenty-five miles a gallon. She was paying nearly seventy bucks a week for gas at the height of the oil spike that summer. "When the world crashed and I got laid off in November," she says now, "we had more money in our pockets at the end of the day with me on unemployment."

It didn't matter where you lived or what you did for a living—in the summer of 2008, the cost of energy almost certainly hit you hard. There was no serious attempt by either the national media or the national political establishment to explain the cause of the problem. Most people assumed it had to do with some combination of shortages and/or increased demand from the Chinese industrial machine, and most TV reports were more than willing to encourage that perception, despite the fact that there were no long lines at the gas stations, no seventies-style rage-fests while waiting for gas, no obvious evidence of scarcity. We were told about a crisis of supply that existed somewhere other than where we could see it—someplace in the abstract.

"I remember watching CNN, and they were trying to tell us about shortages," says Sereda. "They were showing lines in Canada, or somewhere else, someplace."

I mostly spent that summer covering the McCain-Obama presidential campaign for *Rolling Stone,* during which time I heard varying explanations for why this gas price spike was happening, why people like Priscilla were suddenly living out of cars.

McCain, amazingly, spent all summer telling us reporters that the reason for the spike in gas prices was that socialists like Barack Obama were refusing to permit immediate drilling for oil off the coast of Florida.

Like all reporters that summer, I found my attention dominated not by interjections into the commodities market but by a seemingly endless series of made-up controversies involving either warring tribes within the Democratic Party (the Clintonicons versus the Obamaniacs) or blue/red hot-button issues like the Reverend Wright business.

But I do remember that gas was an issue, sort of, and it sort of got talked about by both candidates. I remember being in Kenner, Louisiana, on the night McCain de facto won the nomination and he gave a speech against a hideous puke-green background saying that "no problem is more urgent today than America's dependence on foreign oil." I remember the somber ads McCain started airing that summer talking about how "some in Washington are still saying no to drilling in America."

I remember after that night, the press pool rolled out of its caged-in area after the speech and all us hacks were snickering in the bus about McCain's latest whopper.

"What a bunch of bullshit," one of them, a TV guy I'd known and disliked for years, said. "As if gas prices were going up because of an offshore drilling ban."

"Yeah, nobody's gonna buy that," added another.

This went on for a few minutes. Campaign reporters love to rip the candidates they cover, it's their favorite sport—until the candidate actually walks back into their section of the plane, at which point they go weak in the knees like high school girls and start kissing his skirts like he's the pope. Anyway, at one point of this latest rip session about McCain's drilling gambit, I piped in. "Hey," I said. "Does anyone here actually *know* why gas prices are going up? I sure as hell don't."

There was a brief discussion at this, and theories were offered, but in the end it became clear that none of us in the pool had a fucking clue what was causing the gas spike. I later whispered to another print reporter: "Doesn't that make all of us frauds? I mean, if we're covering this stuff anyway."

His answer: "You're just figuring that out now?"

Later on, I was in Minnesota for the Republican convention in September of that summer and listening—squeezed up against a wall of other suckers with jobs as lousy as mine and with backgrounds in economics as shaky as mine—as McCain explained the problem in explicit terms:

> Senator Obama thinks we can achieve energy independence without more drilling and without more nuclear power. But Americans know better than that. We must use all resources and develop all technologies necessary to rescue our economy from the damage caused by rising oil prices.

How about Barack Obama? He offered a lot of explanations, too. In many ways the McCain-Obama split on the gas prices issue was a perfect illustration of how left-right politics works in this country.

McCain blamed the problem, both directly and indirectly, on a combination of government, environmentalists, and foreigners.

Obama knew his audience and aimed elsewhere. He blamed the problem on greedy oil companies and also blamed ordinary Americans for their wastefulness, for driving SUVs and other gas-guzzlers. I remember him in the pivotal Pennsylvania primary, when Hillary had him running scared for a while, and he was honing a strategy of chalking up the high gas prices to greedy oil companies that, one supposed, were simply bumping up prices to pay for bigger bonuses.

"They have been in fat city for a long time," Obama said in Wilkes-Barre during that campaign, referring to Exxon and other gas companies. "They are not necessarily putting that money into refinery capacity, which could potentially relieve some of the bottlenecks in our gasoline supply. And so that is something we have to go after. I think we can go after the windfall profits of some of these companies."

Both candidates presented the solution as just sitting there waiting to be unleashed, if only one or the other would get the political go-ahead. McCain said the lower gas prices were sitting somewhere under the Gulf of Mexico. Obama said they were sitting in the bank accounts of companies like Exxon in the form of windfall profits to be taxed.

The formula was the same formula we see in every election: Republicans demonize government, sixties-style activism, and foreigners. Democrats demonize corporations, greed, and the right-wing rabble.

Both candidates were selling the public a storyline that had nothing to do with the truth. Gas prices were going up for reasons completely unconnected to the causes these candidates were talking about. What really happened was that Wall Street had opened a new table in its casino. The new gaming table was called *commodity index investing*. And when it became the hottest new game in town, America suddenly got a very painful lesson in the glorious possibilities of taxation without representation. Wall Street turned gas prices into a gaming table, and when they hit a hot streak we ended up making exorbitant involuntary payments for a commodity that one simply cannot live without. Wall Street gambled, you paid the big number, and what they ended up doing with some of that money you lost is the most amazing thing of all. They got America—you, me, Priscilla Carillo, Robert Lukens—to pawn itself to pay for the gas they forced us to buy in the first place. Pawn its bridges, highways, and airports. Literally sell our sovereign territory. It was a scam of almost breathtaking beauty, if you're inclined to appreciate that sort of thing.

The scam was a two-part squeeze. Part one was the commodities bubble, a completely avoidable speculative mania that drove oil prices through the roof. It is perhaps the first bubble in history that badly wounded a mighty industrial empire without anyone even realizing it happened. Most Americans do not even know that it took place. That was part of the beauty of the grift—the oil supply crisis that never was.

This was never supposed to happen. All the way back in 1936, after gamblers disguised as Wall Street brokers destroyed the American economy, the government of Franklin D. Roosevelt passed a law called the Commodity Exchange Act that was specifically designed to prevent speculators from screwing around with the prices of day-to-day life necessities like wheat and corn and soybeans and oil and gas. The markets for these necessary, day-to-day consumer items—called commodities—had suffered serious manipulations in the twenties and thirties, mostly downward.

The most famous of these cases involved a major Wall Street power broker named Arthur Cutten, who was known as the "Wheat King." The government accused Cutten of concealing his positions in the wheat market to manipulate prices. His case eventually went to the Supreme Court as *Wallace v. Cutten* and provided the backdrop for passage of the new 1936 commodity markets law, which gave the government strict watchdog powers to oversee the functioning of this unique kind of trading.

The commodities markets are unlike any other markets in the world, because they have two distinctly different kinds of participants. The first kind of participants are the people who either produce the commodities in question or purchase them—actual wheat farmers, say, or cereal companies that routinely buy large quantities of grain. These participants are called *physical hedgers.* The market primarily functions as a place where the wheat farmers meet up with the cereal companies and do business, but it also allows these physical hedgers to buy themselves a little protection against market uncertainty through the use of futures contracts.

Let's say you're that cereal company and your business plan for the

next year depends on your being able to buy corn at a maximum of $3.00 a bushel. And maybe corn right now is selling at $2.90 a bushel, but you want to insulate yourself against the risk that prices might skyrocket in the next year. So you buy a bunch of futures contracts for corn that give you the right—say, six months from now, or a year from now—to buy corn at $3.00 a bushel.

Now, if corn prices go up, if there's a terrible drought and corn becomes scarce and ridiculously expensive, you could give a damn, because you can buy at $3.00 no matter what. That's the proper use of the commodities futures market.

It works in reverse, too—maybe you grow corn, and maybe you're worried about a glut the following year that might, say, drive the price of corn down to $2.50 or below. So you sell futures for a year from now at $2.90 or $3.00, locking in your sale price for the next year. If that drought happens and the price of corn skyrockets, you might lose out, but at least you can plan for the future based on a reasonable price.

These buyers and sellers of real stuff are the physical hedgers. The FDR administration recognized, however, that in order for the market to properly function, there needed to exist another kind of player—the speculator. The entire purpose of the speculator, as originally envisioned by the people who designed this market, was to guarantee that the physical hedgers, the real players, could always have a place to buy and/or sell their products.

Again, imagine you're that corn grower but you bring your crop to market at a moment when the cereal company isn't buying. That's where the speculator comes in. He buys up your corn and hangs on to it. Maybe a little later, that cereal company comes to the market looking for corn—but there are no corn growers selling anything at that moment. Without the speculator there, both grower and cereal company would be fucked in the instance of a temporary disruption.

With the speculator, however, everything runs smoothly. The corn grower goes to the market with his corn, maybe there are no cereal companies buying, but the speculator takes his crop at $2.80 a bushel. Ten weeks later, the cereal guy needs corn, but no growers are there—so he buys from the speculator, at $3.00 a bushel. The speculator makes money, the grower unloads his crop, the cereal company gets its commodities at a decent price, everyone's happy.

This system functioned more or less perfectly for about fifty years. It was tightly regulated by the government, which recognized that the influence of speculators had to be watched carefully. If speculators were allowed to buy up the *whole* corn crop, or even a big percentage of it, for instance, they could easily manipulate the price. So the government set up position limits, which guaranteed that at any given moment, the trading on the commodities markets would be dominated by the physical hedgers, with the speculators playing a purely functional role in the margins to keep things running smoothly.

With that design, the commodities markets became a highly useful method of determining what is called the spot price of commodities. Commodities by their nature are produced all over the world in highly varying circumstances, which makes pricing them very trying and complicated. But the modern commodities markets simplified all that.

Corn, wheat, soybean, and oil producers could simply look at the futures prices at centralized commodities markets like the NYMEX (the New York Mercantile Exchange) to get a sense of what to charge for their products. If supply and demand were the ruling factors in determining those futures prices, the system worked fairly and sensibly. If something other than supply and demand was at work, though, then the whole system got fucked—which is exactly what happened in the summer of 2008.

The bubble that hit us that summer was a long time in coming. It began in the early eighties when a bunch of Wall Street financial companies started buying up stakes in trading firms that held seats on the various commodities exchanges. One of the first examples came in 1981, when Goldman Sachs bought up a commodities trading company called J. Aron.

Not long after that, in the early nineties, these companies quietly began to ask the government to lighten the hell up about this whole position limits business. Specifically, in 1991, J. Aron—the Goldman subsidiary—wrote to the Commodity Futures Trading Commission

(the government agency overseeing this market) and asked for one measly exception to the rules.

The whole definition of physical hedgers was needlessly restrictive, J. Aron argued. Sure, a corn farmer who bought futures contracts to hedge the risk of a glut in corn prices had a legitimate reason to be hedging his bets. After all, being a farmer was risky! Anything could happen to a farmer, what with nature being involved and all!

Everyone who grew any kind of crop was taking a risk, and it was only right and natural that the government should allow these good people to buy futures contracts to offset that risk.

But what about people on Wall Street? Were not they, too, like farmers, in the sense that they were taking a risk, exposing themselves to the whims of economic nature? After all, a speculator who bought up corn also had risk—investment risk. So, Goldman's subsidiary argued, why not allow the poor speculator to escape those cruel position limits and be allowed to make transactions in unlimited amounts? Why even call him a speculator at all? Couldn't J. Aron call itself a physical hedger too? After all, it was taking *real* risk—just like a farmer!

On October 18, 1991, the CFTC—in the person of Laurie Ferber, an appointee of the first President Bush—agreed with J. Aron's letter. Ferber wrote that she understood that Aron was asking that its speculative activity be recognized as "bona fide hedging"—and, after a lot of jargon and legalese, she accepted that argument. This was the beginning of the end for position limits and for the proper balance between physical hedgers and speculators in the energy markets.

In the years that followed, the CFTC would quietly issue sixteen similar letters to other companies. Now speculators were free to take over the commodities market. By 2008, fully 80 percent of the activity on the commodity exchanges was speculative, according to one congressional staffer who studied the numbers—"and that's being conservative," he said.

What was even more amazing is that these exemptions were handed out more or less in secret. "I was the head of the Division of Trading and Markets, and Brooksley Born was the chair [of the CFTC in the late nineties]," says Michael Greenberger, now a professor at the University of Maryland, "and neither of us knew this letter existed."

of the S&P GSCI. Wheat, on the other hand, only makes up 3.1 percent of the S&P GSCI. So if you invest money in the S&P GSCI and oil prices rise and wheat prices fall, and the net movement of all the other commodities on the list is flat, you're going to make money.

What you're doing when you invest in the S&P GSCI is buying monthly futures contracts for each of these commodities. If you decide to simply put a thousand dollars into the S&P GSCI and leave it there, the same way you might with a mutual fund, this is a little more complicated—what you're really doing is buying twenty-four different monthly futures contracts, and then at the end of each month you're selling the expiring contracts and buying a new set of twenty-four contracts. After all, if you didn't sell those futures contracts, someone would actually be delivering barrels of oil to your doorstep. Since you don't really need oil, and you're just investing to make money, you have to continually sell your futures contracts and buy new ones in what amounts to a ridiculously overcomplex way of betting on the prices of oil and gas and cocoa and coffee.

This process of selling this month's futures and buying the next month's futures is called *rolling.* Unlike shares of stock, which you can simply buy and hold, investing in commodities involves gazillions of these little transactions made over time. So you can't really do it by yourself: you usually have to outsource all of this activity, typically to an investment bank, which makes fees handling this process every month. This is usually achieved through yet another kind of diabolical derivative transaction called a *rate swap.* Roughly speaking, this infuriatingly complex scheme works like this:

1. You the customer take a concrete amount of money—let's say a thousand dollars—and "invest" it in your commodity index. That thousand dollars does not go directly to the index, however. Instead, you're buying, say, a thousand dollars' worth of U.S. Treasury notes. The money you make from those T-bills goes, every month, to your investment bank, along with a management fee.
2. Your friendly investment bank, which might very well be Goldman Sachs, then takes that money and buys an equivalent amount of futures on the S&P GSCI, following the price changes.
3. When you cash out, the bank pays you back whatever you invested, plus whatever increases there have been in commodity prices over that period of time.

If you really want to get into the weeds of how all this works, there's plenty of complexity there to delve into, if you're bored as hell. The monthly roll of the S&P GSCI has achieved an almost mythical status—it is called the Goldman roll, and there are lots of folks who believe that knowing when and how it works gives investors an unfair advantage (particularly Goldman)—but in the interest of not having the reader's head explode, we'll skip that topic for now.

Minus all of that, the concept of index commodity speculation is pretty simple. When you invest in commodities indices, you are not actually buying cocoa, gas, or oil. You're simply betting that prices in these products will rise over time. It might be a short period of time or a long period of time. But that's all you're doing, gambling on price.

To look at this another way—just to make it easy—let's create something we call the McDonaldland Menu Index (MMI). The MMI is based upon the price of eleven McDonald's products, including the Big Mac, the Quarter Pounder, the shake, fries, and hash browns. Let's say the total price of those eleven products on November 1, 2010, is $37.90. Now let's say you bet $1,000 on the McDonaldland Menu Index on that date, November 1. A month later, the total price of those eleven products is now $39.72.

Well, gosh, that's a 4.8 percent price increase. Since you put $1,000 into the MMI on November 1, on December 1 you've now got $1,048. A smart investment!

Just to be clear—you didn't actually buy $1,000 worth of Big Macs and fries and shakes. All you did is bet $1,000 on the prices of Big Macs and fries and shakes.

But here's the thing: if you were just some schmuck on the street and you wanted to gamble on this nonsense, you couldn't do it, because *your* behavior would be speculative and restricted under that old 1936 Commodity Exchange Act, which supposedly maintained that delicate balance between speculator and physical hedger (i.e., the real producers/consumers). Same goes for a giant pension fund or a trust that didn't have one of those magic letters. Even if you wanted into this craziness, you couldn't get in, because it was barred to the Common Speculator.

The only way for you to get to the gaming table was, in essence, to rent the speculator-hedger exemption that the government had quietly given to companies like Goldman Sachs via those sixteen letters.

If you wanted to speculate on commodity prices, you had to do so through a government-licensed speculator like Goldman Sachs. It was the ultimate scam: not only did Goldman and the other banks undermine the 1936 law and upset the delicate balance that had prevented bubbles for decades, unleashing a flood of speculative money into a market that was not designed to handle it, these banks managed to secure themselves exclusive middleman status for the oncoming flood.

Now, once upon a time, this kind of "investing" was barred to institutional investors like trusts and pension funds, which by law and custom are supposed to be extremely conservative in outlook. If you're the manager of a pension fund for Ford autoworkers, it kind of makes sense that when you invest the retirement money of a bunch of guys who spent their whole lives slaving away at hellish back-breaking factory work, that money should actually be buying something. It should go into blue-chip stocks, or Treasury bills, or some other safe-as-hell thing you can actually hold. You shouldn't be able to put that money on red on the roulette wheel.

In fact, for most of the history of the modern American economy, there had been laws specifically barring trusts and pension funds and other such entities from investing in risky/speculative ventures. For trusts, the standard began to be set with an influential Massachusetts Supreme Court case way back in 1830 called *Harvard College v. Amory*, which later became the basis for something called the prudent man rule.

What the Harvard case and the ensuing prudent man rule established was that if you're managing a trust, if you're managing someone else's money, you had to follow a general industry standard of prudence. You couldn't decide, say, that your particular client had a higher appetite for risk than the norm and go off and invest your whole trust portfolio in a Mexican gold mine. There were numerous types of investments that one simply could not go near under the prudent man rule, commodity oil futures being a good example of one.

The system seemed to work well enough for a long period of time, but by the early nineties there was a new class of economists who had come to believe that the prudent man rule was needlessly restrictive. When I spoke with John Langbein, a Yale professor who helped draft the law that would eventually turn the prudent man rule on its head, he was dismissive, almost to the point of sneering, of the prudent man standard.

"It tended to use a sort of . . . widows and orphans standard," he said in an irritated voice.

I paused. "What do you mean by widows and orphans?" I asked.

"Well, what that means is that there was an extreme aversion to loss," he said. "Everyone had to do a lot of bonds and real estate, you understand."

While I was sitting there trying to figure out what was so bad about that, Langbein proceeded to tell me about how he helped draft something called the Uniform Prudent Investor Act of 1994, some form of which would eventually be adopted by every state in the union. The Prudent Investor Act was something of a financial version of the Clear Skies Act or the Healthy Forests Restoration Act, a sweeping deregulatory action with a cheerily Orwellian name that actually meant close to the opposite of what it sounded like.

The rule now said that there was no one-size-fits-all industry standard of prudence and that trusts were not only not barred from investing in certain asset classes, they were actually duty bound to diversify as much as possible.

"It made diversification a presumptive responsibility" of the trust manager, Langbein said proudly, adding, "It abolished all categoric prohibitions on investment types."

This revolution in institutional investment laws on the state level coincided with similar actions on the federal level—including yet another series of very quiet changes to the rules in 2003 by the CFTC, which for the first time allowed pension funds (which are regulated not by the states but by the federal government) to invest in, among other things, commodity futures. At that same time, the CFTC also loosened the rules about who could buy and sell commodity futures. Whereas once upon a time you had to be accredited to trade commodities, there were now all sorts of ways that outsiders could get into the market.

Coupled with the new interpretation of prudence—this notion that institutional investors not only could diversify into other types of investments, but *should* or *had to*—there was suddenly a huge inpouring of money into the commodity futures market.

"Once upon a time, you had to be an accredited investor, and commodities weren't considered an asset class," says Pat McHugh, a trader in natural gas futures who has spent upwards of twenty years watching changes in the market. "Now all of a sudden commodities, it was like it was something you had to have."

Now, with all these changes, the massive pools of money sitting around in funds like CalPERS (the California state employees pension funds) and other state-run pension plans were fair game for the salesmen of banks like Goldman Sachs looking to pitch this exciting new class of investment as a way of complying with what Langbein, the Yalie professor, called the "powerful duty to diversify broadly." These plans tended to be guarded by midlevel state employees with substandard salaries and profound cases of financial penis envy who were exquisitely vulnerable to the bullshit sales pitches of the Wall Street whiz kids many of them secretly wanted to be.

When I told Langbein that I was interested in how it came to be that so many institutional investors ended up putting gobs of money into the commodity futures market in the late part of the last decade, he immediately interjected that such investing was not a good idea for everyone. "Just because it is not prohibited does not mean it's prudent for everyone to invest in oil futures," he said. "Because they are very volatile."

Well, I said, given that they are volatile, what would be an example of a situation in which it *would* be prudent for a trust—something, again, that is supposed to be supersafe—to invest in oil futures?

"Well, um . . . ," he began. "Say . . . Well, let's say the trust portfolio owns real estate that contains oil, real estate whose value fluctuates with oil prices. Then you might want to buy oil futures as a hedge."

Sounds like the kind of extremely common eventuality that is worth completely revamping the regulatory environment for.

Anyway, commodity index investing had one more thing going for it. It was about to be the last thing left on the institutional investment menu that Wall Street did not completely fuck up. By the mid-to-late 2000s the stock market, the consumer credit market, and the housing market had all either imploded spectacularly or were about to implode spectacularly. Those big pools of money had to go somewhere, and the key word that everyone was interested in hearing, after all these disasters, was "safety." And "quality," that was another word. And hell, what seemed more solid than oil? Or sugar? Or wheat?

That was the pitch, anyway. And the banks started hitting that theme really hard in the middle part of the decade.

"Going long on index investing has long been popular in the securities markets," wrote a cheerful Will Acworth in the May 2005 issue of *Futures Industry* magazine. "Now it is coming into fashion in the futures world, and bringing a new source of liquidity to commodity futures contracts."

That probably doesn't make much sense to you now, and wouldn't have made much sense to you in 2005. It did, however, make sense, back then, to the people who managed the great pools of money in this world—the pension funds, the funds belonging to trade unions, and the sovereign wealth funds, those utterly gigantic quasi-private pools of money run by foreign potentates, usually Middle Eastern states looking to do something with their oil profits. It meant someone was offering them a new place to put their money. A safe place. A profitable place.

Why not bet on something that people can't do without—like food or gas or oil? What could be safer than that? As if people will *ever* stop buying gasoline! Or wheat! Hell, this is America. Motherfuckers be eating pasta and cran muffins by the metric ton for the next ten centuries! Look at the *asses* on people in this country. Just let them try to cut back on wheat, and sugar, and corn!

At least that's what Goldman Sachs told its institutional investors back in 2005, in a pamphlet entitled *Investing and Trading in the Goldman Sachs Commodities Index*, given out mainly to pension funds and the like. Commodities like oil and gas, Goldman argued, would provide investors with "equity-like returns" while diversifying portfolios and therefore reducing risk. These investors were encouraged to make a "broadly-diversified, long-only, passive investment" in commodity indices.

But there were several major problems with this kind of thinking—i.e., the notion that the prices of oil and gas and wheat and soybeans were something worth investing in for the long term, the same way one might invest in stock.

For one thing, the whole concept of taking money from pension funds and dumping it long-term into the commodities market went completely against the spirit of the delicate physical hedger/speculator balance as envisioned by the 1936 law. The speculator was there, remember, to serve traders on both sides. He was supposed to buy corn from the grower when the cereal company wasn't buying that day and sell corn to the cereal company when the farmer lost his crop to bugs or drought or whatever. In market language, he was supposed to "provide liquidity."

The one thing he was not supposed to do was buy buttloads of corn and sit on it for twenty years at a time. This is not "providing liquidity." This is actually the opposite of that. It's hoarding.

When an investment banker coaxes a pension fund into the commodities markets, he's usually not bringing it in for the short term. "Pension funds and other institutional investors have extremely long time horizons," says Mike Masters of Masters Capital Management, who has been agitating against commodity speculation for years. He notes, for example, that the average duration of a pension fund's portfolio is designed to match the average employee's years until retirement. "Which could be twenty years, or more," says Masters.

The other problem with index investing is that it's "long only." In the stock market, there are people betting both for and against stocks. But in commodities, nobody invests in prices going down. "Index speculators lean only in one direction—long—and they lean with all

their might," says Masters. Meaning they push prices only in one direction: up.

The other problem with index investing is that it brings tons of money into a market where people traditionally are extremely sensitive to the prices of individual goods. When you have ten cocoa growers and ten chocolate companies buying and selling back and forth a total of half a million dollars on the commodities markets, you're going to get a pretty accurate price for cocoa. But if you add to the money put in by those twenty real traders $10 million from index speculators, it queers the whole deal. Because the speculators don't really give a shit what the price is. They just want to buy $10 million worth of cocoa contracts and wait to see if the price goes up.

To use an example frequently offered by Masters, imagine if someone continually showed up at car dealerships and asked to buy $500,000 worth of cars. This mystery person doesn't care how *many* cars, mind you, he just wants a half million bucks' worth. Eventually, someone is going to sell that guy one car for $500,000. Put enough of those people out there visiting car dealerships, your car market is going to get very weird very quickly. Soon enough, the people who are coming into the dealership looking to buy cars they actually plan on driving are going to find that they've been priced out of the market.

An interesting side note to all of this: if you think about it logically, there are few reasons why anyone would want to invest in a rise in commodity prices over time. With better technology, the cost of harvesting and transporting commodities like wheat and corn is probably going to go down over time, or at the very least is going to hover near inflation, or below it. There are not many good reasons why prices in valued commodities would rise—and certainly very few reasons to expect that the prices of twenty-four different commodities would all rise over and above the rate of inflation over a certain period of time.

What all this means is that when money from index speculators pours into the commodities markets, it makes prices go up. In the stock markets, where again there is betting both for and against stocks (long and short betting), this would probably be a good thing. But in commodities, where almost all speculative money is betting long, betting on prices to go up, this is not a good thing—unless you're one of the speculators. But chances are that's not who you are in this drama. You are far more likely to be Priscilla Carillo or Robert Lukens, dealing with a sudden price hike for reasons you know nothing about.

"It's one thing if you're getting people to invest in IBM or something," says McHugh, the natural gas futures trader. "But wheat and corn and soybeans . . . this stuff actually affects people's lives."

Anyway, from 2003 to July 2008, that moment when Priscilla started living in her car, the amount of money invested in commodity indices rose from $13 billion to $317 billion—a factor of twenty-five in a space of a little less than five years.

By an amazing coincidence, the prices of all twenty-five commodities listed on the S&P GSCI and the Dow-AIG indices rose sharply during that time. Not some of them, not all of them on the aggregate, but all of them individually and in total as well. The average price increase was 200 percent. Not one of these commodities saw a price decrease. What an extraordinarily lucky time for investors!

In and around Wall Street, there was no doubt what was going on. Everyone knew that the reason the price of commodities was rising had to do with all the new investor flows into the market. Citigroup in April 2008 called it a "Tidal Wave of Fund Flow." Greenwich Associates a month later wrote: "The entry of new financial or speculative investors into global commodities markets is fueling the dramatic run-up in prices."

And the top oil analyst at Goldman Sachs quietly conceded, in May 2008, that "without question the increased fund flow into commodities has boosted prices."

One thing we know for sure is that the price increases had nothing to do with supply or demand. In fact, oil supply was at an all-time high, and demand was actually falling. In April 2008 the secretary-general of OPEC, a Libyan named Abdalla El-Badri, said flatly that "oil supply to the market is enough and high oil prices are not due to a shortage of crude." The U.S. Energy Information Administration (EIA) agreed: its data showed that worldwide oil supply rose from 85.3 million barrels a day to 85.6 million from the first quarter to the second that year, and that world oil demand dropped from 86.4 million barrels a day to 85.2 million.

Not only that, but people in the business who understood these things knew that the supply of oil worldwide was about to increase. Two new oil fields in Saudi Arabia and another in Brazil were about to start dumping hundreds of thousands more barrels of oil per day into the market. Fadel Gheit, an analyst for Oppenheimer who has testified before Congress on the issue, says that he spoke personally with the secretary-general of OPEC back in 2005, who insisted that oil prices had to be higher for a very simple reason—increased security costs.

"He said to me, if you think that all these disruptions in Iraq and in the region . . . look, we haven't had a single tanker attacked, and there are hundreds of them sailing out every day. That costs money, he said. A lot of money."

So therefore, Gheit says, OPEC felt justified in raising the price of oil. To *45 dollars a barrel*! At the height of the commodities boom, oil was trading for three times that amount.

"I mean, oil shouldn't have been at sixty dollars, let alone a hundred and forty-nine," Gheit says.

This was why there were no lines at the gas stations, no visible evidence of shortages. Despite what we were being told by both Barack Obama and John McCain, there was no actual lack of gasoline. There was nothing wrong with the oil supply.

But despite what Wall Street players were saying amongst themselves, the message to potential investors was very different. In fact, it still is. Banks like Goldman Sachs continually coaxed new investors into the commodities market by arguing that there would be major disruptions to the world oil supply that would cause oil prices to spike. In the beginning of 2008, Goldman's chief oil analyst, Arjun Murti, called an "oracle of oil" by the *New York Times,* predicted a "super spike" in oil prices, forecasting a rise in price to two hundred dollars a barrel.

Despite the fact that there was absolutely no evidence that demand was rising or supply falling, Murti continually warned of disruptions to the world oil supply, even going so far as to broadcast the fact that he owned two hybrid cars, adding with a straight face: "One of the biggest challenges our country faces is its addiction to oil."

This was a continuation of a theme Goldman had shamelessly pimped for years, that high prices were the fault of the piggish American consumer; in 2005 a Goldman analyst even wrote that we wouldn't know when oil prices would fall until we knew "when American consumers will stop buying gas guzzling sport utility vehicles and instead seek fuel efficient alternatives."

"Everything that Goldman cooked up or predicted, by hook or by crook, it happened," Gheit says. "[Goldman and Morgan Stanley] pushed these prices up."

All of these factors contributed to what would become a historic spike in gas prices in the summer of 2008. The press, when it bothered to cover the story at all, invariably attributed it to a smorgasbord of normal economic factors. The two most common culprits cited were the shaky dollar (investors nervous about keeping their holdings in U.S. dollars were, according to some, more likely to want to shift their holdings into commodities) and the increased worldwide demand for oil caused by the booming Chinese economy.

Both of these factors were real. But neither was any more significant than the massive inflow of speculative cash into the market.

The U.S. Department of Energy's own statistics prove this to be the case. It was true, yes, that China was consuming more and more oil every year. The statistics show the Chinese appetite for oil did in fact increase over time:

YEAR	CONSUMPTION (barrels per year)
2002	1,883,660,777
2003	2,036,010,338
2004	2,349,681,577
2005	2,452,800,000
2006	2,654,750,989
2007	2,803,010,200
2008	2,948,835,000

If you add up the total increase between each of those years, i.e., the total increase in Chinese oil consumption over the five and a half years between the start of 2003 and the middle of 2008, it turns out to be just under a billion barrels—992,261,824, to be exact.

During the same time period, however, the increase in index speculator cash pouring into the commodities markets for petroleum products was almost exactly the same—speculators bought 918,966,932 barrels, according to the CFTC.

But it was almost impossible to find mention of this as a cause for the spike in gas prices anywhere in the American media, which at the time was focused on more important things, like the geographical proximity of Bill Ayers to Barack Obama, or whether Geraldine Ferraro was being racist or just stupid when she said that Obama would not be winning the nomination "if he were a white man."

I was out there, covering the campaign, and what I remember was a lot of ginned-up anger between working-class Democrats (who supported Hillary) and yuppie Democrats (who supported Obama), a lot of anger emanating from female Hillary supporters (at a Hillary rally in Washington, DC, I saw two women tear an Obama sign away from a young girl and call her a "traitor"), and in general a lot of noise about things that, in retrospect, had nothing to do with anythin... all.

While most of the country was talking about Reverend ... superdelegates, media coverage of the soaring gas price... nonspecific and unconvincing. The *New York Times* ... stories on high gas prices and specifically blamed ... demand," which it called "the relentless driver ... That was at the end of February 2008, wh... record high of $100.88 a barrel. ...eral fac-

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While most of the country was talking about Reverend Wright and superdelegates, media coverage of the soaring gas prices was curiously nonspecific and unconvincing. The *New York Times* ran one of the first stories on high gas prices and specifically blamed the rise on "global oil demand," which it called "the relentless driver behind higher prices." That was at the end of February 2008, when oil hit what was then a record high of $100.88 a barrel.

A CNN story back in March 2008 called "Gasoline Price Spike Has Only Just Begun" told us that the reason for the surge was, well, because this is what always happens in between winter and summer:

> The price of gasoline usually increases this time of year. Several factors contribute to the runup: Low refinery output due to mainte-

nance, a switch from winter to pricier summer blends, and the looming high-demand summer driving season.

Politicians blamed the high prices on a variety of factors—the most ridiculous perhaps being Kentucky senator Mitch McConnell blaming high prices on an automatic gas tax instituted by his electoral opponent, Bruce Lunsford, in the Kentucky state legislature thirty years before.

By late spring and early summer the stories about the gas spike were more common, but quite often they seldom even mentioned a cause for the price disruptions. In most cases it was simply assumed that the high prices were caused by too much consumption, that Americans were going to have to change their habits if they wanted to survive the high costs.

When gas soared to over four dollars a gallon in May, *USA Today* ran a story called "Gas Prices Rattle Americans" that talked about the sobering—perhaps even positive—effect the high prices had had on the national psyche:

> The $4 mark, compounded by a sagging economy, could be a tipping point that spurs people to make permanent lifestyle changes to reduce dependence on foreign oil and help the environment, says Steve Reich, a program director at the Center for Urban Transportation Research at the University of South Florida.
>
> "This is a more significant shift in behavior than I've seen through other fluctuations in gasoline prices," he says. "People are starting to understand that this resource . . . is not something to be taken for granted or wasted."

There is nothing new about the political press in America getting a story wrong, especially a financial story. But what was unique about the gas spike story was that it was an issue that profoundly affected the lives of virtually everyone in the country, was talked about heatedly by both parties and by pundits in the midst of a presidential election year, and yet as far and as wide as you search, you simply will not find much of a

mention anywhere about the influx of new commodity index money as a potential cause of this crisis.

And you barely heard it on the Hill. Several different congressional committees decided to hold hearings on the high gas prices, including Joe Lieberman's Homeland Security and Governmental Affairs Committee and the House Agriculture Subcommittee on General Farm Commodities and Risk Management. At these hearings there were some voices, like those of Mike Masters and Fadel Gheit, who tried to talk about the real causes of the crisis, but the headlines generally followed the pronouncements of the CFTC's chief economist, Jeffrey Harris, who said that the whole problem stemmed from normal supply and demand issues.

In written testimony before both committees in May 2008, Harris convincingly dismissed the notion that speculators played any role in the high prices.

"All the data modeling and analysis we have done to date indicates there is little evidence to suggest that prices are being systematically driven by speculators in these markets," he said. "Simply put, the economic data shows that overall commodity price levels . . . are being driven by powerful fundamental economic forces and the laws of supply and demand." He cited, as evidence of "fundamentals," the increased demand from emerging markets, decreased supply due to "weather or geopolitical events," and a weakened dollar.

The government's chief economist on the matter blamed the oil spike on the *weather*!

Even weirder was the fact that Harris was apparently so determined to keep any suggestion that speculation played a role in the problem out of the hearings, he even called up at least one witness to try to get him to change his mind.

"This guy tried to shake me down!" says Gheit, still incredulous at the story. He recounts a bizarre phone call in which Harris called up the Oppenheimer analyst, put him on speakerphone so that another colleague could listen in, and proceeded to tell Gheit that he had no evidence that speculation played a role in the crisis and that maybe he should consider this before he testified.

Gheit, who actually thought the call was coming from a staffer in Senator Carl Levin's office at first, found himself wondering what the hell was going on. "I said, 'Whose side are you on?' " As the phone call progressed, Gheit began to consider other possibilities. "I was sure it was someone from Goldman Sachs or Morgan Stanley. That's how weird it was."

It would be a full year before the CFTC under the Obama administration would admit that Harris's analysis was based on "deeply flawed data" and that speculators played a major role in the crisis.

But by then it was too late to stop what happened in 2008. Oil shot up like a rocket, hitting an incredible high of $149 a barrel in July 2008, taking with it prices of all the other commodities on the various indices. Food prices soared along with energy prices. According to some estimates by international relief agencies—estimates that did not blame commodity speculation for the problem, incidentally—some 100 million people joined the ranks of the hungry that summer worldwide, because of rising food prices.

Then it all went bust, as it had to, eventually. The bubble burst and oil prices plummeted along with the prices of other commodities. By December, oil was trading at $33.

And then the process started all over again.

The oil bubble, taking place as it did smack-dab in the middle of a feverish presidential campaign, was really a textbook example of how our national electoral politics and our media watchdogs are inadequate to address even the most glaring emergencies.

When you have a system with an electorate divided up into two fiercely warring tribes, each determined to blame the country's problems on the other, it will often be next to impossible to get anyone to even pay attention to a problem that is not the fault of one or the other group. Moreover it is incredibly easy to shift blame for the problem to one of those groups, or to both of them, if you know how to play things right—which happened over and over again in this case.

Throughout the spike, America accepted almost without question

the notion that our problems were self-inflicted, caused by our obscene consumption of oil. It was a storyline that appealed in different ways to the prejudices of both of the two main political demographics.

It naturally appealed to the left, which for entirely logical reasons saw an evil in America's piggish dependence upon petroleum and had just spent five long years protesting an invasion of Iraq seemingly driven by our political elite's insatiable thirst for oil.

Oil consumption for progressives was, in fact, at the heart of two of their core protest issues: America's rapacious militarism and its environmental irresponsibility. America had bowed out of Kyoto. We had supported dictatorships in Saudi Arabia and Kuwait and (once upon a time) Iran in our hunger for oil and had toppled or tried to topple regimes in oil-rich countries like Iraq and Venezuela for seemingly the same reason.

More to the point, America was the birthplace of the SUV—the evil symbol of American oil gluttony that in one conveniently boxy package tied together all of the symbolic frustrations of the American progressive. It had a vaguely militaristic symbolism (the domestic Hummer was a modified military vehicle). It was driven unashamedly by big-assed conservatives and their teeming white-trash families who openly thumbed their noses at environmental concerns—witness the bumper stickers often seen plastered to the hugest SUV brands, with messages like "I'll Give Up My SUV When Al Gore Gives Up His Limo" and "Hybrids Are for Pussies" and "My SUV Can Beat Up Your Prius."

The last sticker had a particular sting, given that just as driving a big gas-guzzling SUV was a mode of political expression for conservatives, driving hybrids was one of the easiest ways for progressives to "have an impact" on the causes they cared about. The San Francisco political activist Robert Lind in the early part of the decade had encouraged opponents of SUVs and people who drove energy-efficient vehicles to download bumper stickers that read, "I'm Changing the Climate! Ask Me How!" He was followed by the Evangelical Environmental Network, which started its "What Would Jesus Drive?" bumper sticker campaign in 2002, which prompted a *60 Minutes* story about the anti-SUV backlash.

In short, the idea that Americans consumed too much oil had enormous traction with American progressives, among other things because it happened to be true.

So it wasn't at all hard to sell Democratic voters on the notion that the oil spike was related to overconsumption. In fact, the whole consumption issue had enormous symbolic import for Democratic voters, and it wasn't a surprise when presidential candidates started working vague references to overconsumption—divorced, of course, from specific policy proposals—into speeches that were supposedly addressing the gas price issue. When Obama went to Oregon in May 2008, right in the middle of the oil bubble, he specifically referenced SUVs, as I would hear him do over and over again that summer. "We can't drive our SUVs and eat as much as we want and keep our homes on seventy-two degrees at all times" was one of his favorite lines.

He consistently got cheers with that line, and to me it seemed obvious that these were angry cheers, cheers directed at the "other side," who consumed as much as they wanted and thought the Prius was for fags.

Meanwhile conservatives bought the supply-disruption storyline because it fit in seamlessly with the story of capitalist efficiency thwarted by regulators, tree-huggers, and OPEC. An oil spike caused by shortages justified the Iraq invasion and put the blame on environmentalists who blocked drilling in the Alaska National Wildlife Refuge and the outer continental shelf and those other dickwads who were always sacrificing American jobs on the altar of the spotted owl.

Those same SUVs that had once been bedecked with bumper stickers justifying the vehicle itself were, in the summer of 2008, starting to be plastered with new stickers that saw their owners' right to consume as a protest cause. "Drill Here, Drill Now!" was one sticker we saw a lot that summer.

What made this important was the fact that the new Obama administration really changed very little when it came to the problem of index speculation. The public was never focused on it, not really. When Obama nominated the new CFTC chief, Gary Gensler, a former Goldman executive and lieutenant to Bob Rubin who had been partially responsible for deregulating the derivatives market in 2000, few people even blinked.

This was news for specialists and experts in the industry, of course (Gheit compared putting Gensler in charge of the CFTC to "making a former legalization advocate the drug czar"), but America is no longer a country that cares about experts. In fact, it hates experts. If you can't fit a story into the culture-war storyline in ten seconds or less, it dies.

That's what happened to the oil speculation problem. Although the CFTC would finally, in August 2008, admit that speculation was a serious issue, and Gensler himself would demonstrate what appears to be a real conversion on the core problems, the root causes remained basically unchanged—so much so that at this writing, oil prices are once again soaring, once again thanks to prodding from the same old cast of villains.

In a weekly newsletter distributed to its own investors only, given to me by a source in the industry, Goldman Sachs in October 2009 repeated its classic "oil is going up because of the fundamentals" act.

"We believe oil prices are poised to move higher, with the catalyst likely to be evidence of rebounding diesel demand," the company wrote. "The normal Christmas retail seasonal effect suggests we should see a rebound in diesel demand in mid to late October to restock shelves." The newsletter continued later: "Crude oil prices have been both volatile and range bound, but poised to break out."

That particular analysis memo was released on a Monday (October 19), just after oil had crept back above $70 a barrel for the first time in more than a year. By that Wednesday the price of crude had gone up seven whole dollars. By Friday, October 23, it was closing at $81.19 a barrel.

What is interesting about this Goldman memo is not how obviously full of shit it is, but the disclaimer that is hidden in the very back of it.

On the very last page of the newsletter, in tiny print, Goldman wrote, under the heading "General Disclosures," the following:

> Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients and our proprietary trading desks that reflect opinions that are contrary to the opinions reflected in this research. Our asset manage-

> ment area, our proprietary trading desks and investing businesses may make investment decisions that are inconsistent with the recommendations or views expressed in this research.
>
> We and our affiliates, officers, directors, and employees, excluding equity and credit analysts, will from time to time have long or short positions in, act as principal in, and buy and sell, the securities or derivatives, if any, referred to in this research.

Translated into English, Goldman can take your investment order and do anything they want with it, no matter how conflicted they might be. They might be recommending that you buy oil futures for "fundamental reasons," like the holiday shopping season or some such bullshit, but in the fine print they admit that, "from time to time," they might have long positions themselves as they make that recommendation.

Here, in this one document, is laid bare the whole basic stratagem behind the oil bubble. The big investment banks convince the ordinary investor that oil prices are going up because of "fundamentals," then they get all that money coming in, at which point their predictions about prices going up actually come true. Then they ride in with their own bets and make a fortune, front-running the massive flows of capital pouring into the market. Meanwhile, we all end up paying $4.50 a gallon for gas, just so these assholes can make a few bucks trading on what amounts to inside information.

"The reality is that if Goldman is successful enough marketing commodity index swaps to institutional clients they can make their research self-fulfilling," says one commodities trader. "Because those money flows that Goldman's marketing efforts create can move prices by themselves."

This story is the ultimate example of America's biggest political problem. We no longer have the attention span to deal with any twenty-first-century crisis. We live in an economy that is immensely complex and we are completely at the mercy of the small group of people who understand it—who incidentally often happen to be the same people who built these wildly complex economic systems. We have to

trust these people to do the right thing, but we can't, because, well, they're scum. Which is kind of a big problem, when you think about it.

And here's the punch line: bubbles like the one we saw in 2008 are only one-half of the oil-price scam. Because *taking* your money through the indirect taxation of high energy and food prices, and reducing you to beggary as you struggle to pay for them, is only half of the job. What these clowns did with all that cash they siphoned from you and what they did to take advantage of your newfound desperation is the other end of the story.