Book Reviews by Ian Robertson

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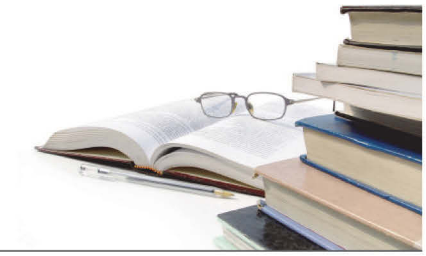

Title: ***The Big Short***

Author: **Michael Lewis**

First Edition: **W.W. Norton & Company (2010)**

Reviewed: **April 2013**

"A most entertaining read."

Rating:
★★★★★
Out of 5 Stars

The Big Short is the best kind of investment book: it's entertaining, with larger than life characters in unimaginable situations; it's edifying (you won't even realize you're being schooled until after the fact); and it's a story no-one else has told (*The Greatest Trade Ever* comes closest). Readers can get structured narratives about the recent crisis through excellent tomes like Sorkin's *Too Big To Fail* or economist's critiques in books such as Stiglitz's *Freefall*, but you'll likely not find another book like this one; a stunning and jaw-dropping account by one of the best authors in the business.

Lewis is the same author who burst onto the scene with his first book, the instant classic *Liar's Poker*, and followed up with a string of excellent books, including *Moneyball* and *The Blind Side*. *The Big Short* is Lewis at his best.

Lewis understands the investment business like the insider he was, but this book is very much from the perspective of a critic. It is much more direct in its criticism of the financial industry than was *Liar's Poker*. In that book, he similarly crafted a terrific story, but with a bemused "can you believe we did that?" tone. In this book, Lewis taps Main Street's anger, and to great effect (sample quote: "... he was the walking embodiment of the bond market, which is to say he was put on earth to screw the customer."). It's hard for folks on Main Street to know exactly who to blame, and exactly what Wall Street did to cause such a mess, and Lewis lays out in clear and entertaining detail who did what.

Who comes off looking badly? Wall Street firms, rating agencies (Moody's, S&P, Fitch), the fixed income market, the SEC, Ken Lewis (no relation) of Bank of America, and the financial system in general.

Who are the characters? Steve Eisman, Dr. Mike Burry, and Greg Lippmann, none are household names, but all memorable characters who become important cogs in the collapsing Wall Street machine. John Paulson (who, as referenced above, made the greatest trade ever) is featured in a small way, and is perhaps the only protagonist with any celebrity.

Eisman's story is centered on his bets against Collateralized Debt Obligations, or CDOs, an esoteric type of bond backed by assets such as sub-prime mortgages. The second narrative thread follows Burry and the evolution of his fund in its bets against the housing bubble, and the impatience of his investors as the sub-prime defaults were slow to materialize. Lippmann's story is even more unusual; an insider, the head sub-prime mortgage trader at Deutsche Bank, and one of the earliest to figure out the likely end to the sub-prime story. Lippmann is willing to tell his story to anyone who would listen; unfortunately, that wasn't his employer.

As in *Liar's Poker*, Lewis weaves his remarkable story around memorable characters, and through the telling of his story, he imparts an incredible amount of industry detail and insight into a very readable text. For example, in a few pages Lewis conveys the essence of options mispricing, something it takes Nassim Taleb a book to do. The story contains both detail and context; individual transactions and broad commentary on the financial system; and neither individuals nor the system come off looking good.

For those looking for Wall Street conspiracy theories, Lewis provides a different angle than *Too Big To Fail*. Goldman Sachs' sale to Burry of credit default swaps (CDS) on sub-prime mortgage bonds earned them a juicy sales commission, but it was an instrument they didn't back directly ("Triple A" rated AIG backstopped most). Burry knew this, but was focussed on profiting from the obvious (to him) sub-prime credit bubble. When the credit bubble started becoming clearer to the investment banks, they too looked to load up on CDSs, with Goldman becoming one of the larger purchasers. It didn't occur to Goldman that the CDS securities might themselves be a bubble, and that the primary issuer of them (AIG) might itself face bankruptcy. Only the U.S. government's bailout of AIG prevented Goldman and others from being caught in a classic squeeze: paying out on defaults and facing a bankrupt insurer on the other end. Goldman was lucky.

Lewis again on the dealers' modus operandi, "When you talk to the dealers, you are getting the view from their book. Whatever they've got on their book will be their view." "All that mattered was what Goldman Sachs and Morgan Stanley decided should matter." Whether it was true or not. When all the Wall Street firms were riddled with sub-prime exposure, they all had to say they were fine, there was no exposure. It wasn't fine, and it took time and effort for the shorts to prove them wrong.

A remarkable story of outsiders tilting at Wall Street when they had limited knowledge, access, and a system working against their interests. Turns out Wall Street was wrong.