There must have been mixed emotions in the marbled parlours of JP Morgan, when they learned that Gillian Tett was writing a book which centres on the role played in the genesis of the financial crisis by their innovative credit derivative team of the 1990s.

It is not always an unalloyed pleasure to have Tett on your case. When I was at the Bank of England in the mid 1990s she had her claws into the Old Lady, for reasons I have happily forgotten. Our lugubrious press officer, a man with a good sense of history, would report gloomily on each phase of what he described as “the Tett offensive”, as the Bank’s positions came under fire from unpredictable directions.

There are some echoes here of those old battles. While Paul Tucker is quoted admiringly, Governor Mervyn King is variously described as “stubbornly dogmatic” and “cerebral, owlsh”. Of course there’s no defence against “cerebral”. In Britain the rudest thing you can say about anyone is that they are clever and read books. But I am rather fond of owls, as it happens, and stubbornness is not always a vice in a central banker, it seems to me.

In fact the folks at JP need not worry unduly. She is rather kind to the central cast of characters, contrary to what the racy subtitle would have you expect. The thesis of “Fool’s Gold” is that a small group of clever quants at JP Morgan invented credit derivatives: all the dangerous acronymic creatures, CDOs, CLOs and the like, that we have come to know as the crisis has evolved. But it was other, greater fools, in other banks, who misunderstood and misused them.

The inventors seem to have done all their creative work at a series of off-site meetings in Florida resorts (close those places down at once), punctuated with jolly japes as fun-loving managing directors were thrown in the pool by drunken rocket scientists. Tett would clearly love to have been a fly on the wall at these events, which fill most of us with fear and loathing, and at times implies that she was. Obviously the FT does not provide enough corporate bonding fun for its reporters.

She introduces us to the cast of characters who made it all happen: Bill Winters, Peter Hancock and Bill Demchak in the States, Blythe Masters and Tim Frost in London. Winters and Masters are still with the bank: the others have moved on.
Masters is still the high priestess of securitisation as chair of the Securities Industry and Financial Markets Association in New York, though now when she speaks in public “in deference to the dark mood of the times, she wears a sombre, chocolate-brown suit, instead of her usual jewel-toned hues”. Such subtle semiotics are not available to men:

it’s not fair. Frost emerges as a kind of Macavity the mystery cat: now a firework inventor, now a trader, then creatively salvaging an SIV, and today an advisor on restructuring to the Bank of England.

The innovations which emerged from the fertile minds of this talented team were supposed to make the world safer. They allowed risks to be sliced and diced and spread around the globe, to be held by those best able to bear them. This narrative, assiduously promoted by the banks, was generally accepted by the financial authorities at the time. In its 2006 annual report the IMF noted that “The dispersion of credit risk by banks to a broader and more diverse set of investors….has helped to make the banking and overall financial system more resilient...improved resilience may be seen in fewer bank failures”.

But in the wrong hands these fireworks proved to be, well, explosive. Tranched and squared, insured by monolines, triple A rated by S & P and Moody’s, tucked away in SIVs, they looked as safe as houses, and indeed were, except that the houses concerned were falling sharply in value, and the over-gearied occupants were non-status borrowers. Many of the investors, including titans like Merrill, Citi and UBS, had not understood the risks, and lost their shirts (and red braces too). The rest is familiar history to readers of Ms Tett’s columns.

JP Morgan, the original begetter on the Tett reading, sailed through the turmoil relatively unscathed, under Captain Dimon. They had not loaded up their balance sheet with super-senior tranches, as did most of their competitors, and were largely SIVless. If Bill Winters’ hindsight testimony is to be believed, “I could never work out why anyone thought SIVs were a good idea.”

What blame should attach to the manufacturers, if their fireworks fall into the wrong hands? Tett rather leaves the question hanging, and also leaves open the issue of whether it would be possible to create a regulatory environment which allows proper use of such complex creations, while guarding against the worst risks of mis-selling and misapplication. There is no market today for the racier instruments, but securitisation will surely return in some form, so regulators and central banks will need an answer before too long.

The best journalism, they say, is the first draft of history. There is no doubt that Gillian Tett’s reporting of the securitisation market is in that category. Her background in anthropology has given her insight into the human (well, ok, they are bankers, but prick them and they bleed) dimension of the crisis, to add depth
to her understanding of the statistical quirks of the Gaussian cupolas. This close reading of what happened in a corner of the financial world will be of great value to those who seek a more comprehensive assessment of the crash in due course. It is well-written, as we have come to expect. The broader judgments later in Fool’s Gold, on the role of central banks and regulators are more provisional, I think. As with the tortoise and the hare, the owl might just catch up with the mystery cat one day.