



“Gold-Plated Sachs?”

Almost three years since the onset of the financial and subsequent economic crisis, United States' banks once again braced themselves for a massive sell-off in share values. The New York Stock Exchange rumbled on news of alleged fraud at one of the few Wall Street giants to prosper during the crisis, Goldman Sachs. Controversies including bonus rows and as some would describe it “deal-making that precipitated the financial crisis”, are not new to the grand old institution; however, a scandal of this magnitude was certainly farfetched. Indeed, the company is accused of skillfully making money at the start of the financial crisis in 2007 to the tune of USD1 billion, involving dodgy mortgages, powerful hedge funds and extraordinarily boastful emails. In light of these developments, it seems that the United Kingdom and several European economies are not the only ones with volcanic activity but there is also what seems to be a cloud of legal and political ash hovering above Goldman Sachs.

With a history tracing back to 1869, it took just one sentence in a 2007 email to trigger a well-timed complaint by the Securities and Exchange Commission (SEC) against Goldman Sachs and one of the bank's vice presidents on 16 April. In the midst of a heated debate in the US Senate on financial regulation, the SEC accused “them of marketing born-to-lose mortgage-backed securities without making full disclosure to unwary investors.” At the forefront of the scandal, Stanford-educated Fabrice Tourre is alleged to have written a “smoking-gun e-mail as he chortled over the audacity of the scheme to help a leading client, the hedge fund run by John Paulson, place a \$1 billion bet against the housing market.” Further to this, the SEC cited in its complaint that the email included, “the whole building is about to collapse anytime now...only potential survivor, the fabulous Fab...standing in the middle of all these complex, highly leveraged, exotic trades that he created without necessarily understanding all the implications of these monstrosities!!!!” It's certainly times like these that one wonders if former Federal Reserve Chairman Paul Volcker was right when he stated, “the most important financial innovation that I have seen in the past 20 years is the automatic teller machine.”

With an avalanche of news coming to light over the past few weeks, the SEC has a task on their hands proving that one of the most profitable companies in Wall Street did indeed defraud collateralized debt obligations' (CDOs) investors in particular IKB Deutsche Industriebank AG and ABN Amro Bank NV. In a nutshell, the case is reduced to whether there was a “false statement or a material omission that made statements materially misleading” on the part of Goldman Sachs. Despite the SEC's not so great track record with prosecuting such complicated cases, this case is expected to be more delicate due to the fact that foreign regulators are involved coupled with the high possibility that these investigations will expand to other financial institutions involved in the CDO business. According to the SEC's enforcement chief, “the product was new and complex, but the deception and conflicts are old and simple.”

Obviously, at Goldman's testimony before the Senate Permanent Subcommittee on Investigations held on 26 April, the company's executives argued they did not place a massive bet against the housing market but conceded in 2007 they made a half a billion dollar profit on their mortgage investments. Indeed, five present and two former Goldman officials held their ground in hours of contentious testimony, unflinchingly and to some, arrogantly defending their conduct and denying that the Wall Street investment bank helped cause the near-meltdown of the nation's financial system.

Unsurprisingly, Standard & Poor's (S&P) equity analysts downgraded Goldman Sachs to a "sell", citing concerns that the civil, and now reported criminal investigations, into the bank "muddles" its future business. In a report, S&P analysts cut their price target on Goldman from USD190 a share to USD140 a share. Analysts said that while fraud charges are "traditionally difficult to prove," just the threat is enough to cause damage to Goldman's business. "We think the risk of a formal securities fraud charge, on top of the SEC fraud charge and pending legislation to reshape the financial industry, further muddies Goldman's outlook," said S&P equity analyst. Goldman shares have fallen more than 15% since the SEC announced its civil fraud charges against the firm.

On top of this, it's not a good sign that executives inside Goldman Sachs are reportedly discussing life after CEO of Goldman Sachs, Lloyd Blankfein. The *Wall Street Journal's Deal Journal* has gone so far as to discuss more specific candidates for either the chairman or CEO position.

According to a Reuters report, President Barack Obama was cited as indicating that the current Goldman scandal was attributable to Wall Street's "furious efforts" to fight tighter regulation and that the US was doomed to another financial crisis if reforms were not implemented. All these factors have certainly heightened confidence that the US will approve restrictions on how big banks operate. Obama indicated that the legislation is expected to significantly improve the current flawed regulatory structure, "despite the furious efforts of industry lobbyists" to try to weaken it and blamed the financial meltdown and the recession that followed on a "failure of responsibility" by both Washington and Wall Street.

Whether the odds are in favor of the SEC or Goldman Sachs, the timing of the scandal could not have come at a worse time with much of the damage being done before there is any resolution on this matter. The potential widespread ramifications are expected to fuel uncertainty at a time when the fragile global economy is slowly creeping towards recovery.

FINANCIAL & ECONOMIC INDICATORS

As at 6 May 2010

<u>Exchange Rate/US\$</u>	<u>Closing Value</u>	<u>Previous Week</u>
Yen	90.58	94.03
Euro	1.26	1.32
Jamaica	89.33	89.28
Guyana	ND	ND

<u>Commodity Prices</u>	<u>Closing Value</u>	<u>Previous Week</u>
Crude oil (US\$/bbl)	77.11	85.17
Natural Gas (US\$/mmbtu)	3.97	4.24
Gold (US\$/Troy Ounce)	1,208.57	1,166.85

Eurobond Indices (As at 06-05-10)

JP Morgan EMBI+ (Basis points)	323
JP Morgan Central America and Caribbean Index (CACI) (YTD return %)	7.50

<u>Policy Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
United States	0.25	0.25
Euro Zone	1.00	1.00
Japan	0.10	0.10
Brazil	9.50	9.50
Trinidad	5.00	5.00
Jamaica	10.50	10.00
Barbados	2.50	2.50

<u>Market Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
US 90-day T-Bill	0.11	0.16
US 10-Yr Treasury	3.40	3.73
3-month UK Libor	0.68	0.68
Japan 90-day T-Bill	0.28	ND
Brazil 90-day T-Bill	9.95	10.29
TT 90-day T-Bill	1.15	1.15
Jamaica 90-day T-Bill	9.73	10.18
Barbados 90-day T-Bill	3.26	3.26

Sources: Bloomberg, J.P. Morgan, CMMB Research Center, Central Bank of Trinidad and Tobago, Bank of Jamaica, Central Bank of Barbados

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