

**THE ECSTASY OF HYPER-CONSUMPTION, A DISEASE WITHOUT A CURE,
AND THE ONSLAUGHT OF THE SUB-PRIME MORTGAGE DEBACLE OF**

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The collapse of the sub-prime mortgage market in the summer and fall of 2007 brought about the predictable “weeping, wailing, and gnashing of teeth.” People and institutions were ruined, foreclosures abounded; and, accordingly, investigations were called for and blame had to be distributed. To round up the most likely suspects, investigators needed only look to the rapacious capitalists crowding the halls of mortgage firms, the mortgage departments of banks, brokerage houses, and real estate firms of all varieties. Home buyers, it goes without saying, were to be treated as victims, and government/ private lending agencies were rarely expected to play the role of villain – though there had been some stories of an “accounting scandal” at Freddie Mac within the past year. [1]

The aforementioned analysis would no doubt satisfy many readers. It is so easy to picture nefarious lenders luring victims with promises of low monthly payments followed by “balloons here” and “balloons there” – and, essentially, it’s all too complex

to explain [2] Information on mortgage applications might have been checked; but, then again, maybe not. Why not let applicants claim any income they choose to claim? Indeed, why not print out bogus “W -2”s on your favorite Hewlett Packard printer? This is a story so easy to picture in the mind’s eye. Why challenge so comfortable a view?

In this particular case, I much prefer to think back to the wonderful cartoon character Pogo who became famous for the observation: “We have met the enemy and he is us.” The root cause of this collapse, it can be argued, rests with the American home buyer and the insatiable lust for larger and larger homes. Houses in current American culture have become *trophies*, the bigger the better. No matter that you can’t afford a stick of furniture or a few shrubs, how big is the box? In a society that has been drowning in “materialism” forever, it is arguable that we have now moved up a notch to “hyper- consumption” – indeed, there is now a book on the subject by Benjamin Barber of the University of Maryland. [3] At the risk of belaboring the obvious, none of this could have happened without the lust of prospective buyers *signing on the bottom line*.

Beyond some thoughts regarding the star-struck consumer, it will also be worth noting the extent to which federal/private lending agencies have become thick as flies – please notice I did not say “thick as thieves.”

SOME HISTORICAL BACKGROUND ON MATERIALISM

Seminal thinkers have been railing against the evils of materialism for about as long as anyone can remember – to little or no avail, of course.

Aristotle in his *Nicomachean Ethics* noted that many men would measure you by your wealth and possessions, but that these were coarse and vulgar people and you should pay them no mind.

In the Gospel According to Mark 8:36 the question is raised: “What will it profit a man if he should gain the whole world and lose his own soul?”[4]

Emerson looked at the world about him and had the insight to observe: “Things are in the saddle and ride mankind.”

Emerson’s friend Thoreau sought a more simple and reflective life by hiding out for a very brief time at Walden Pond.

Tocqueville writing in *Democracy in America* in the 1830s was bemused by the extent to which Americans ran about helter-skelter in a mad passion to turn a dollar.

If we jump ahead 150 years to our current era, we can hear very similar admonitions, no doubt with very similar results:

Christopher Lasch in *The Culture of Narcissism* demonstrated considerable social insight in this provocative jeremiad against self-indulgence.

E.F. Schumacher in *Small is Beautiful* speaks of “Buddhist Economics” and consuming less. Even daring to suggest that less is more – more or less. [5]

Wendell Berry has a cottage industry selling books that promote the simple life.

Mitch Albom in *Tuesday’s With Morrie*, possibly the most popular book on college campuses in the past decade, learns that good friends and quality relationships (including with a former professor dying of ALS) are to be valued more highly than money and national recognition gained as a prominent sports writer.

In sum, from Aristotle to Albom warnings against the nefarious influence of materialism have been abundant, and yet most of these voices might be correctly characterized as “voices crying in the wilderness.”

IT GETS WORSE

Arguably, the quest for “more stuff” knows no limits. A friend of mine who has been teaching psychology at my college for the past 40 years reminds me, periodically, that where “greed” is concerned, there are never any limits. Never imagine that the lust of a greedy person has been satiated. [6] (Forget the Law of Diminishing Returns.) Accordingly, a bad situation can always get worse. Recently, as noted earlier, a social critic by the name of Benjamin Barber gave it a name: *hyper-consumption*. [7] If we grasp the meaning of this new label, we can begin to see how homebuyers went down the path they did.

What are some of the better examples of hyper-consumption in the American economy? Barber cites \$10 billion spent on bottled water annually, often by consumers who actually understand that this water is not coming from some wonderful spring in the Colorado Rockies or the Blue Ridge Mountains of Virginia. If it’s bottled water with an upscale label, then it’s good stuff, even if it’s coming from a garden hose in Bayonne, New Jersey. [8]

What about evidence from advertising analysis that TV programmers are beginning to target babies between the ages of 6 months and one year old in order to shape viewing habits and thereby one day influence buying patterns a few years down the road. Does this strike anyone as a tad extreme? [9]

Does the need for every family to drive a Hummer, a very large SUV, or at least something resembling a tank more than an auto explain our extraordinary consumption of

oil – which, in turn, places more pressure on the United States President and State Department to play a very large role in the geopolitics of the Middle East? Is this an example of hyper-consumption that makes a political difference? (Two Gulf Wars twelve years apart suggest the answer might be yes.) [10]

What can we discern from the fact that the 20 highest grossing movies coming out of Hollywood in 2006 were all targeted for the 11-14 year old audience? What does this say about *adults* who might enjoy a movie? What chance does this provide for films made in India or Sweden or some other foreign land on a serious subject? Can the “art” of filmmaking in America ever hope to look beyond Shrek and Harry Potter? [11]

What is the significance of spending \$1 billion per year on Cialis and Viagra? What precisely does one do with “an erection lasting more than four hours” in the average retirement community? But, obviously, we are all “entitled.” Just what America needs: 10,000,000 eighty year olds with STDs. (Socially Transmitted Disease.) [12]

Barber asks many good questions – some of which have already been raised by foreign observers (and he repeats the question): Why does America have only two political parties, but 200 brands of cereal? Is the ubiquitous mall (same stores in every town) replacing the public square or the town hall in American life? Sadly, we may already know the answer to these questions before we ask them.

Incidentally, one of the more amusing recent examples of hyper-consumption is the emergence of Freshman Year Abroad. A college-directed year abroad was initially crafted for the relatively more mature juniors and seniors. However, with the current ethos of “I want all the goodies up front and I want them now,” welcome to Freshman Year Abroad! [13]

COULD PUBLIC/PRIVATE LENDING AGENCIES ADD TO THE MANIA?

When it comes to placing blame for the mortgage debacle could it be the case that somehow most major lending agencies frequently managed to fly below the radar when guilt and blame were being assigned? After all, who could take issue with a private/public body allegedly created to promote home ownership? How could anyone challenge a provider of the American dream? To what extent can the average citizen begin to name even a few of the many alphabet agencies that provide mortgages?

There is GNMA known as “Ginnie Mae” – created by F D Roosevelt in 1938. (The author admits to holding Ginnie Mae stock.)

There is FNMA known as “Fannie Mae”- as of July 08 in very serious trouble, and by September of 2008 in a state of total collapse.

There is “Freddie Mac” noted earlier in the paper for their accounting scandal in 2007, covered in depth by *The Wall Street Journal* – also on the verge of collapse, and by September of 2008 in total collapse. (Preliminary investigation reveals that both Fannie and Freddie did an extraordinary job of spreading money around Washington, and apparently owned Representative Barney Frank, Democrat of Massachusetts and Senator Chris Dodd, Democrat of Connecticut, outright – to say nothing of Senator Chuck Hagel, Republican of Nebraska) So, if you know/own enough Congressmen, apparently there are no rules. In one rather famous confrontation over regulation, Barney Frank shouted at his critics: “You hate poor people” – You hate poor people.” End of discussion.

There is the “FHA” or the Federal Housing Administration

There is the Department of Veterans Affairs or the “VA” that provides mortgages.

There is the Department of Agriculture’s “RHS” or Rural Housing Service

There is the Department of Housing and Urban Development

There is an Office of Public and Indian Housing or “PIH”

If this list seems a bit lengthy, consider on the local level many programs designed to get employees to buy homes in the neighborhood where they work:

School Districts (Lancaster, PA) have mortgages to place “teachers in the neighborhood.”

Cities have low cost mortgages that plant “cops in the neighborhood.”

Franklin & Marshall College (Lancaster, PA) has a program for “professors in the hood.”

Do you begin to get the picture? Who in the world could hope to monitor all this—such that mortgage money would be let out in a responsible fashion? Do folks running these agencies and programs actually worry about distributing the money carefully? Maybe a subliminal purpose, in some cases, might be to just “spread a little bit of money round the hood.” Was everyone put on earth with a burning desire to make a monthly mortgage payment? [14] I doubt this very much. Should someone ask some hard questions here?

THE ROLE OF THE SUB-PRIME MORTGAGE MARKET

Similar to the government agencies, the sub-prime market expanded the opportunities for home ownership. In the decade following World War II, for example, with the aid of “G.I. Mortgages,” home ownership for households in the United States

climbed from 45% to 65%; but then hovered around 65% for the next 35 years.

Obviously, people with limited disposable income were shut out. Put another way, roughly a third of the population was “condemned” to renting. [15] This “condemned to renting” argument sometimes sounds a bit silly when you consider the tens of thousands of affluent folks in places such as New York City, Philadelphia, Baltimore, and Washington, D.C. who **choose to rent**.

The sub-prime market, logically, offered mortgages to lower income/higher risk families – understandably, with higher interest rates, and a greater rate of default. Some of these families were “graduates” of rent subsidy programs. [16] Many were directed and encouraged by 4,000 Community Based Organizations that provided competent counselors on home buying. [17]

In recent years, perhaps the overused “adjustable rate mortgages,” “interest only mortgages,” and “negative-amortization mortgages” contributed to rising default rates in the sub-prime market. From the consumer’s perspective, loss of a job and medical problems were the primary reasons for default. [18] Accordingly, the sub-prime market found a niche for itself in the modern American economy – albeit an unregulated one.

UNFORTUNATE RECENT IDEAS THAT GREW UP IN ALL MORTGAGE MARKETS AMONG MANY HOME BUYERS

Back in the “bad old days” a potential homebuyer needed either 20% of the price of the house as a down payment or a GI mortgage. More recently, however, it has been said that so many young people were “cash poor.” Accordingly, if they had little or no cash, but both had jobs, the jobs came to justify the granting of the mortgage. (Two young people with jobs can’t be all bad.

Another new “development” could be seen in the notion that there need not be any iron clad relationship between income and the cost of the house purchased. In the dark past there was a “rule of thumb” suggesting that a monthly mortgage payment should not exceed a certain percentage of your income, perhaps 28 to 31%. In the new age, however, thanks to creative financing, all these old guidelines could be cast aside – as outdated as buggy whips and high-button shoes! A clever financier with a sharp pencil could make most anything possible. You simply had to *believe*. [19]

Another contributor to the “bubble,” if that’s what this was, were the rising expectations in a democratic society. Obviously, we are all entitled to the very best, the very finest, the largest, etc. Toll Brothers of Philadelphia, one of the nation’s largest home builders, pioneered in building mini mansions that became known as “McMansions.” Full of upscale appliances, these homes sold for anywhere from \$400,000 to \$1,000,000 depending on the location and cost of the lot.

A mortgage broker recently told me the story of an elderly couple, once affluent, but now down on their luck financially, who came to her for advice on purchasing a home. The broker “ran the numbers” and told the couple that in their newly unfortunate financial state they could only afford to pay about \$180,000 to \$190,000 for a house. The woman being told this was deeply offended, flew into a rage, and stomped off – never to speak with the broker again. What was wrong with this broker? She dared to tell the truth! [20] (Is it possible that some or many brokers were rewarded for the *amount* of money they put out the door – as opposed to the *quality* of the loans? Indeed, some insiders in the mortgage business spoke of NINJA loans. “NINJA loan” today stands for:

no income, no job or assets, NINJA.) Of course, there are also “Liar’s Loans” in which all numbers on the mortgage application are simply invented.

The point of these three paragraphs is to note that the “new age” approach to putting people into homes was, at times, silly or almost nonsensical. I remember a “creative” mortgage broker arguing with me some eight months ago that exotic mortgages were not really a problem. The “real” problem was that these same homebuyers were running \$80,000 in credit card debt. [21] Obviously, as always, no one ever admits to wrong doing. It’s always someone else’s fault. This particular debacle really does lend itself to pointing the finger at the next guy – as there are many “next guys.” And, of course, the “sub-prime mortgage market,” by definition, is a different world.

The late Dr. Edward M. Gramlich, a former Federal Reserve governor, cited earlier, has argued for the need “to better protect consumers against predatory lending practices and toughen the regulation of mortgage lenders and banks, calling the process “confusing, costly and far less than optimal.” As early as 2002 he argued that the “practices of sub-prime lenders, such as charging excessive fees and refinancing just to collect more fees “jeopardize the twin American dreams of owning a home and building wealth.” Gramlich put this in book form in 2007 in *SubPrime Mortgages: America’s Latest Boom and Bust*. [22]

OVER THE TOP, OVER THE TOP, OVER THE TOP – OR – WHAT IS WALL

STREET FOR?

Just when it seemed that the mortgage market could not get any zanier, mortgage originators discovered that they could take *literal bundles* of high risk mortgages, have them stamped “AAA” by Moody’s and Standard and Poor’s, and sell them in totally unlimited quantities to Wall Street that in turn sold this stuff globally. The ratings agencies justified their AAA ratings on the rarified assumptions that (1) housing prices would rise forever (there is no bubble), and that (2) homebuyers would faithfully make their mortgage payments – even beyond the early “sweetheart” phase of the agreements. And so it came to pass that bundles of mortgages with AAA ratings were marketed near and far. There was no particularly good reason to doubt Moody’s and Standard and Poor’s. Accordingly, financial managers in small towns in Switzerland bought this paper; later admitting they really had no idea what they were buying!

A FUNNY THING HAPPENED WHILE WE WORRYING ABOUT AND WORKING ON THE MORTGAGE CRISIS

Between February and September of 2008 it was entirely possible for citizens and “financial types” to imagine that, even with the failure of Bear Stearns and the problems at Fannie Mae and Freddie Mac, the mortgage market and financial markets were engaged in some process of self-correction. (Alan Greenspan in his new book *The Age of Turbulence*, New York: Penguin, 2007, makes this argument.) However great the dislocation, it was not important enough to bring down the entire house of cards. But this assumption was made prior to **Black Monday** September 15 and **Blacker Monday** September 29 and **Black Wednesday** October 15. September 15, 2008, **Black Monday**, witnessed (1) a drop in the DOW of 504 points, (2) the failure of Lehman Brothers (roughly 158 years old), (3) the Bank of America takeover of Merrill Lynch, and (4) the

desperate outcries of AIG for \$50,000,000 in capital, bailed out a day later by the federal government. **Black Monday** witnessed a drop in the DOW of 777 points. **Black Wednesday** witnessed a drop in the DOW of 733 points, despite recent Congressional approval of a “Bailout” or “Rescue” and a move by European countries to guarantee citizen bank deposits. Throughout October of 2008 the market kept tumbling – with occasional modest rebounds. By October 24 the DOW had plummeted 38% -- from 14,000 to 8,691. On December 1, 2008 the DOW dropped another 679 points.

DARE ANYONE DRAW A CONCLUSION

Beset with a series of corporate scandals in the past decade, it must be hard for most anyone to get overly exercised about the latest debacle. Obviously, whatever it is, it will surely blow over in a few weeks. The great surprise, this time around, are the developments of **Black Monday**, September 15, 2008, that vividly demonstrate how a problem in the sub prime mortgage market grew and grew far beyond anything that anyone seemed to be capable of imagining. Of course, a few years ago no one could have fully appreciated the implications of hedge funds, derivatives, and “abusive” or conspiratorial short selling.... Perhaps like characters in a Dreiser novel, we are self-destructing without any idea of precisely what we are doing to ourselves, but rest assured that everything is leveraged!

Recently I suggested to an economist that Wall Street might be in need of “moral rearmament.” He responded by asking: “What sort of moral rearmament do you have in mind? – as though like the writings of William James there might be “varieties” of moral rearmament.

THE MYSTERIOUS \$700 BILLION BAILOUT

In the face of the greatest economic and financial dislocation since the 1930s the president, the congress and the president-elect all seemed to agree concerning the need for a major federal “bailout” in November of 2008, and so it was that the House and Senate agreed to appropriate \$700 billion to rescue mortgages, banks, etc. The beauty of this development was the inability of most anyone to explain how this money was to be used. In a better world, congressmen would be able to explain this tactic to the good folks back home in their district. Obviously, the rest of this episode has yet to be written.

POSTSCRIPT – OUTRIGHT FRAUD

While this paper has emphasized the culpability of the consumer/borrower and the blame that might accrue to the endless federal/private lending agencies that often appear to answer to no one, it would be horrendously naïve to not say a word about fraud. At the end of January of 2008 a SEC investigation focused on “Swiss Bank UBS AG and US investment banks Morgan Stanley, Merrill Lynch, Bear Stearns, as well as bond insurer MBIA.” [23] At the same time the FBI was looking at fraud in loan origination. The FBI estimated they had about 1,200 active cases and that included some 321 criminal complaints or indictments. [24] By the time we get to the end of the story we can be certain that fraud will have played a role.

Note: In June a new book appeared by Richard Bitner, *Money for Nothing: Confessions of a Subprime Lender* (New York: Wiley, 2008.) Bitner explains how home loans were made to bad credit risks by “manipulating their credit reports” and even printing bogus W2s to make incomes appear higher than they actually were.

END NOTES

1. The “accounting scandal” at Freddie Mac, unfortunately, included some very difficult political/racial issues that surely will not be addressed in this paper.
2. There is no question but that the average consumer signing on the bottom line had little chance to understand the intricacies of the “new finance.”
3. Benjamin Barber, *Consumed: How Markets Corrupt Children, Infantilize Adults, and Swallow Citizens Whole* (New York: Norton, 2007.)
4. The New Testament includes other comparable quotes on materialism.
5. Schumacher’s material works very well in teaching undergraduates.
6. This wisdom comes from Professor Paul Dennis who teaches Abnormal Psychology at Elizabethtown College.
7. Barber.
8. Ibid, 3.
9. Ibid.
10. Ibid, 4.
11. Ibid.
12. Ibid, 5.
13. See *The Wall Street Journal* for January 22, 2008.
14. To say that the burden of monthly mortgage payments are for everyone is about as silly as arguing that everyone, obviously, loves the same flavor of ice cream.
15. Edward M. Gramlich, *Subprime Mortgages: America’s Latest Boom and Bust* (Washington, DC: Urban Institute Press, 2007.), 1.

16. Ibid., 10.

17. Ibid., 30.

18. Ibid., 68

19. The most important thing to believe is that all the old rules of economics and finance are now obsolete. Surely, a new generation is entitled to more benign parameters and rules.

20. This story was related by Rose Dennis who had been working for Wells Fargo.

21. This gem of wisdom came from “Kathy,” a mortgage broker in Lititz, PA.

22. See *The Washington Post* for September 5, 2007. See also, Edward M.

Gramlich, *Subprime Mortgages: America’s Latest Boom and Bust*.

23. Wall Street firms in FBI subprime probe/News.com.au Business.

24. Ibid.

Note: In late July of 2008 Dick Army observed that the Freddie Mac/Fannie Mae episode looked like “Enron on steroids.”

Note: The ultimate cure for “hyper consumption,” of course, is an economy in ruins. On the eve of the election, November 3, 2008, Paul Kruger of *The New York Times* wrote a column entitled “The Consumers Capitulate.” He noted that “real consumer spending fell at an annual rate of 3.1% in the third quarter” . . . and that “real spending on durable goods fell at an annual rate of 14%.” Stated a bit differently, the American consumer has not had a religious experience and converted to a life of monasticism and self-denial. Rather, the American consumer, for the moment, has run out of cash and credit . . . or perhaps he has been stunned by the real estate concept of “negative equity” – meaning that he owes \$700,000 on a house with a market value of \$600,000.