<u>Bill Clinton a prime suspect for starting meltdown</u>

Andrew Main
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We are now sitting in the wreckage of the biggest lending bust the world has ever seen.

And there's some merit in trying to pinpoint where it all began.

And among the prime suspects is former president Bill Clinton's decision in 1999 to put pressure on lenders to widen the pool of home borrowers in the US.

An article in The New York Times on September 30, 1999, laid it all out in what now looks like crystal detail.

"In a move that could help increase home ownership rates among minorities and low-income consumers, the Fannie Mae corporation is easing the credit requirements on loans that it will purchase from banks and other lenders," the article, by Steven Holmes, began.

"The action, which will begin as a pilot program involving 24 banks in 15 markets, including the New York metropolitan region, will encourage those banks to exchange home mortgages to individuals whose credit is generally not good enough to qualify for conventional loans. Fannie Mae officials say they hope to make it a nationwide program by next spring.

"Fannie Mae, the nation's biggest underwriter of home mortgages, has been under increasing pressure from the Clinton administration to expand mortgage loans among low and moderate income people and felt pressure from stock holders to maintain its phenomenal growth in profits."

It's like listening to a cockpit voice recorder extracted from the tail of some aircraft wreck.

The next paragraph notes that banks and mortgage companies had been pressing Fannie Mae to help them make more loans to so-called sub-prime borrowers.

Why?

Because such people "can only get loans from finance companies that charge much higher interest rates".

Don't they say that the road to Hell is paved with good intentions? That story, whose first three paragraphs were reproduced verbatim, was all about the US government trying to help. On top of that, the banks and mortgage companies thought they were doing the borrowers a favour because otherwise they would have been hit with higher rates.

What has happened now, with a million empty houses in the US and no sign of prices bottoming out, is the logical consequence of ill-considered positive discrimination on one side of the ledger.

Latinos and African Americans are the biggest minorities who were talked about in the article, as it later made clear, and as we know they now make up a disproportionate number of mortgage defaulters in the US housing market. There have been instances of people who don't like minorities saying "I told you so" about what's happened, but there's a very strong argument that it would have happened to any supposed beneficiary of rule bending.

If the lenders had focused on helping Southern good ol' boys, by some quirk, we'd probably be looking at an army of confused and unhappy Southern ex-home owners having to park their rocking chairs on other people's verandas. The iron rule of commerce that was ignored was that money should always be lent to people who are going to be able to pay it back, regardless of any other consideration.

"Home ownership has, in fact, exploded among minorities during the economic boom of the 1990s," the 1999 article stated. "The number of mortgages extended to Hispanic applicants jumped by 87.2 per cent from 1993 to 1998," it continued, noting that for African Americans the number had jumped by 71.9 per cent and Asian Americans 46.3 per cent. By comparison, the number of non-Hispanic whites (as they are called) who received loans for homes increased by 31.2 per cent.

That final number said it all. Even the laggards, Mr and Mrs Middle America, saw their home ownership jump by almost a third in a decade, at a time when the US economy was booming, but by every account the real incomes of people in the lower third of the economy moved up by a smaller percentage than the upper two-thirds.

A new book called Confessions of a sub-prime Lender by Richard Bitner and just released in Australia by John Wiley & Sons, stays right away from the positive discrimination issue, but provides a cornucopia of other horror stories.

"Until 1998 home prices and income increased in relative proportion to each other, which mean housing affordability remained largely unchanged," writes Bitner, who admits to having sold out of his sub-prime mortgage origination business shortly before last year's meltdown.

"Over the next 10 years, the balance between the two became skewed. While income grew marginally, home prices skyrocketed, which created an affordability gap," he writes.

He says Wall Street investment firms started securitising the loans in 1993, but that's a saga for another day.

Back at The New York Times, the award for prescience goes to a man called Peter Wallison, a resident fellow at the American Enterprise Institute.

"From the perspective of many people, including me, this is another thrift industry growing up around us," he was quoted as saying.

"If they fail, the government will have to step up and bail them out in the same way it stepped up and bailed out the thrift (savings and loan) industry."

The S&L cleanup of the early 1990s is believed to have cost the US government around $US200 billion, which seemed like a lot at the time. It doesn't look such a big deal now.