Have We Got an (Underwater) Deal for You!

by John Hoefle

Nov. 20—With every passing week, it becomes more apparent that the Obama Administration has been a complete failure. Wipe away the grimy layers of hype and spin, and all you find is catastrophe, a galloping, accelerating disaster.

The touted success of the stimulus program is exemplary: Behind all the lying claims lie non-existent jobs, created in non-existent Congressional Districts, in a non-existent recovery. Washington keeps talking about its success, but the people who have to live with the results know better. People who are worried about where their next mortgage payment—or their next meal—will come from, are not impressed with press releases.

A raft of reports released recently show how the American standard of living is being rapidly destroyed, while certain Wall Street interests are being propped up. In medical terms, the Obama Administration's policies amount to letting the patient die, while keeping the tumor on life support.

Home, Crashing Home

One of the fundamental requirements for human progress is shelter. Every person, every family, needs a place to live. Civilization depends upon it, and one of the marks of a civilized society is that it never lets such an essential requirement become the playground of speculators. But that is exactly what we did, in allowing the financial markets to turn housing into "financial assets," driving home prices into the stratosphere.

Ultimately, the prices became unsustainable, the bubble popped, and housing prices began to fall. Rather than welcome this return toward "normalcy," the Bush and Obama administrations rushed to save the speculators. They did this by launching a slew of bailout schemes designed to arrest the decline of home values, in the hopes of salvaging the values of trillions of dollars of securities based upon mortgage debt, and of preventing a chain-reaction collapse of the entire global monetary system.

They did not move to save the families stuck with hugely overpriced mortgages. They moved to save the values of the financial assets leveraged on top of those mortgages. They moved to save the tumor!

The result of this betrayal, for the population, has been a disaster. More and more people are falling behind in their mortgage payments, foreclosures are soaring, and increasing numbers of Americans are homeless. Tent cities of the sort last seen in the Great Depression, are becoming commonplace.

A survey released this week by the Mortgage Bankers Association reported that, as of Sept. 30, nearly 1 in 10 households (9.6%) was a month or more behind in their mortgage payments, and that 1 in 11 households (8.9%) was either 90+ days past due, or in foreclosure. Overall, 4.5% of residential mortgages were in foreclosure, a 50% jump from September 2008.

Not surprisingly, the subprime loans fared the worst, with just over 1 in 4 (26%) homeowners being 30 days or more behind in their payments; but delinquencies on prime loans are also rising sharply: 1 in 14 (6.8%) of prime mortgages is 30 days or more behind, and 1 in 8 (12.4%) of all prime adjustable-rate mortgages is delinquent. All of these rates are rising sharply.

As this mortgage meltdown accelerates, the government agencies being used to subsidize the bailout are taking heavy losses. The Federal Housing Administration, which is used to turn private mortgages into government-guaranteed paper, is hemorrhaging money. One in seven of its loans is a month or more past due, and 3.3% are in foreclosure. The FHA's losses from this boondoggle are so large that it has wiped out its reserves, and will soon have to turn to the Treasury for cash.

Then there are Fannie Mae and Freddie Mac, the two government-sponsored enterprises which were effectively nationalized last year. Since the current phase of the financial crisis began in July 2007, Fannie Mae has lost $120 billion, and Freddie Mac $68 billion. That combined $188 billion is equivalent to the 14th-largest bank in the United States losing all of its assets.

Taken together with Ginnie Mae (the Government National Mortgage Association), these mortgage subsidies are going to cost taxpayers mind-boggling amounts of money down the road, if sane heads don't reverse this stupidity.

We should also note the rather obvious point that the foreclosure rate tends to increase with the unemployment rate, and that both are quickly rising. With 1 million people facing the loss of unemployment benefits in January 2010, on top of the job losses, it's going to get even uglier.

Commercial Real Estate, Too

The banks may have been successful in transferring much of their mortgage losses onto the taxpayer through such schemes, but commercial real estate is proving more problematic. Fitch Ratings recently projected that U.S. banks could face defaults on $110 billion in commercial property loans they hold, but we find that figure highly optimistic, since $138 billion of such loans is already in default. With commercial real estate prices down by more than 40% in the past two years, more than half of the $1.4 trillion in commercial mortgages maturing in the next five years is underwater (meaning, the property is worth less than the amount of the mortgage). The delinquency rate is rising here, too, up five-fold, to 5%, in the last year.

Those who were foolish enough to buy properties at the peak of the market are really suffering. Exemplary is the case of Tishman Speyer and BlackRock, which paid $5.4 billion to buy Stuyvesant Town and Peter Cooper Village—Manhattan's largest apartment complex—in 2006, only to see the value of the property fall to $1.8 billion. The Tishman-BlackRock partnership had hoped to plug the hole by raising rents, only to be slapped down by New York State courts, which ruled that rent hikes on some 4,350 apartments violated the law. Fannie Mae and Freddie Mac own $1.5 billion in commercial mortgage-backed securities backed by deeply troubled loans.

Tishman and BlackRock are hardly alone. Goldman Sachs recently unloaded 158 condos near Miami for about one-third of their land and construction costs; and Bank of America is suing Maguire Properties, the largest landlord in downtown Los Angeles, for skipping payments in August, September, and October. The properties in question were bought by Maguire for $2.9 billion in 2007. Deutsche Bank is taking a beating on the unfinished Cosmopolitan Resort & Casino in Las Vegas, which it seized in foreclosure next year. Commercial real estate exposure is also sinking many smaller banks, including most of the banks which have failed this year.

Shut It Down!

Delusions die hard. Just this week the Comptroller of the State of New York released a glowing report touting how the big four investment-banking operations on Wall Street had made $23 billion in profits so far this year, compared to $40 billion in losses last year. The top six bank holding companies did even better, with $51 billion in profits this year versus $62 billion in losses last year.

These "profits" are illusory, the product of Federal subsidies, accounting fraud, hidden losses, and unbridled criminality. The attempt to keep these big zombies alive, is a major factor in the disintegration of the rest of the economy. Far from helping the U.S. economy, the bailout is killing it. How many people must lose their jobs and their houses, to keep Wall Street going? Isn't it time we put a stop to this monstrosity?

We must return to what works, the American System. Put the monetary system through bankruptcy, write off the speculative debt, reorganize the banks, return to a credit system, with a Four-Power alliance. It's time for the LaRouche Plan.

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