Photo: Federal Reserve

The Greenspan years

Reflecting on Michael Hudson's judgment of Alan Greenspan as the global elite's economic mythmaker, **Ed Dodson** concludes his own three-part assessment of the Greenspan legacy

IN HIS final year in the Presidency, Bill Clinton delivered the annual *State of the Union* message to the nation. Among the achievements of his administration that he highlighted was the elimination of the annual budget deficit and a small reduction in the total national debt. "Now, if we stay on this path, we can pay down the debt entirely in just 13 years and make America debt-free for the first time since Andrew Jackson was President in 1835", he declared. Given that the US government's accounting practices were—and always have been—divorced from what any auditor would demand of a business, the actual circumstance of the time is impossible to discern. In September of 2000, David Walker, the Comptroller of the United States cautioned the nation that more remained to be done than had been accomplished:

"From a fiscal perspective, we aren't out of the woods yet. The future surpluses that are the current subject of intense debate are based on projections. Just three years ago we had projected deficits for as far as the eye could see. In addition, we know that we face a demographic tidal wave that can swamp our future fiscal picture and return us to the days of growing deficits if we are not prudent about our actions today. This demographic tidal wave is not a projection, it is a fact because the individuals who comprise it are already living, and many are rapidly approaching their normal retirement eligibility dates."

In a speech delivered in December 2000 at the Federal Reserve Bank in Philadelphia, Edward M Gramlich, a member of the Fed's board of governors, highlighted the fact that "conventional home purchase mortgage lending to low-income borrowers increased nearly 75 percent between 1993 and 1998", and that "conventional mortgages to African-Americans increased 95 percent over this period, and Hispanics 78 percent". It seems rather ironic today to read his next statement:

"Much of this increased lending can be attributed to the development of the subprime mortgage market. The Department of Housing and Urban Development (HUD) reports that the number of subprime home equity loans has gone from 80,000 in 1993 to 790,000 in 1998, an 880 percent increase. This rapid growth has given access to credit to consumers who have difficulty in meeting the underwriting criteria of 'prime' lenders because of blemished credit histories or other aspects of their profile. This access gives people from all walks of life a shot at the American dream—owning a home and getting capital gains."

Despite these gains, there was disturbing information coming to the surface. An industry long plagued by fraud and theft was experiencing these problems at a previously unimaginable level of sophistication. The players were rightfully described as predators and their practices described as predatory lending. Neither regulation nor law enforcement have significantly mitigated, let alone eliminated, the problems. Investigative hearings held in 1997 by the HUD resulted in a detailed report to the US Congress, but no legislation. Financial literacy programs developed by the Fed, the FDIC (Federal Deposit Insurance Corporation) and other organisations are reaching only a small percentage of those most susceptible to the marketing pressures applied by agents of the predatory lending companies.

Subprime mortgage originations reached \$90 billion in 1996. The Fed's own analysis of data gathered under the Home Mortgage Disclosure Act (HMDA) confirmed that from 1993 to 2000 the number of subprime purchase money mortgage loans increased from around 16,000 to over 306,000. By 2000 the number of subprime second mortgage loans exceeded an annual volume of 658,000. In a speech delivered by Alan Greenspan in March that year, the Fed chairman acknowledged the existence of "abusive lending practices that target specific neighbourhoods or vulnerable segments of the population and can result in unaffordable payments, equity stripping, and foreclosure." A report issued in November of 1999 by the General Accounting Office (GAO) took the Fed to task for its failure to examine the lending practices of subprime lending companies owned by the nation's banks. The Fed has been grappling with this aspect of their regulatory responsibilities ever since.

By 2002 subprime mortgage originations represented roughly 10 percent of the total dollar volume of residential mortgage loans closed. Reported mortgage loan fraud, already out of control, skyrocketed. As a result of litigation, two lenders—Household Finance and Ameriquest Mortgage Company—agreed to \$800 million in restitution to consumers.

Still, US homeowners continued to refinance existing mortgage debt and draw equity out of their properties. Some 8 million mortgage loans were refinanced in 2002, 12 million in 2003. This represented nearly one of out every six homeowners.

The stresses on the US economy and on many American people were intensifying. Every year the number of home foreclosures and bankruptcies hit historic highs.

In 2005, Ravi Batra made a case for Alan Greenspan's prominent role in the unravelling of the US economy in his book, *Greenspan's Fraud*. Batra argued that the Fed under Greenspan oversaw the demise of a large portion of the middle class. Batra traces Greenspan's complicity back to the early 1980s, when he supported increases in the payroll tax to help reduce the Reagan budget deficit. This was the first step in eliminating the progressivity of the Federal income tax. He had summarised his views on Greenspan in an earlier interview:

"Greenspan's fault was his poor understanding of economics. He thought that the productivity jump resulting from the adoption of information technology generated high profits, which lubricate stock markets. But he forgot that when wages fail to keep pace with productivity, then the economy needs explosive debt growth to maintain profit growth. But debt growth cannot increase forever; so a stock market crash was inevitable. That is why all speculative bubbles pop in the end."

And, in the end we are left with our own conclusion whether Michael Hudson's assessment is more accurate than that of Ravi Batra. Has Greenspan been an active and knowing agent of the privileged elite? Or, is he basically an economist who possesses an extremely limited understanding of how markets function and how fiscal and monetary policies affect markets? Perhaps the best answer is that he is a good deal of both. In any event, we are once again at the end of the 18-year land market cycle, poised for another collapse while our government officials and central bankers do what they can to place the blame elsewhere. L&L

Edward J Dodson is Director of the US-based School of Cooperative Individualism and author of Discovery of First Principles. *Parts I & II of 'The Greenspan years' were published in* L&L *1221 & 1222. 'Mr Greenspan's myth' by Professor Michael Hudson, to which 'The Greenspan years' is a response, was published in* L&L *1220.*