

Creating Liquidity Out of Spatial Fixity

The Secondary Circuit of Capital and the Restructuring of the US Housing Finance System

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Introduction

This chapter examines the current crisis within the US housing finance sector as an illustration of the contradictions of capital circulation as expressed in the tendency of capital to annihilate space through time. In his classic works, Karl Marx argued that one of the distinctive logics of capital accumulation is the tendency by capital to eliminate the spatial and temporal barriers to the realization of exchange values, to reduce to a minimum the time that it costs to produce and sell commodities. One of the major obstacles or barriers to realization of profit, as Marx noted, is the time involved in producing commodities, transporting them to market, and exchanging them for profit. In the case of land and housing, real estate's time in circulation can distend for months or years as capital is tied up for varying periods of time in the process of production and exchange, and hence cannot immediately be returned back to the capitalist in its enhanced form, M' . The longer the turnover time of real estate capital, the smaller the amount of surplus value. Speeding up and increasing the velocity of the circulation of capital and reducing the turnover time derives from the logic of the accumulation process. According to Marx,

While capital must on one side strive to tear down every spatial barrier to intercourse, i.e. to exchange, and conquer the whole world for its market, it strives on the other side to annihilate this space with time, i.e. to reduce to a minimum the time spent in motion from one place to another. The more developed the capital ... the more does it strive for an even greater extension of the market and for greater annihilation of space by time. (1973: 539)

Over the century Marx's ideas and theories have influenced countless scholars interested in understanding the growth-oriented, technologically dynamic, and crisis-prone nature of capitalism and its effects on urban space. During the 1960s and 1970s, Henri Lefebvre and David Harvey drew attention to the physical landscape and built environment as a source of and barrier to capital accumulation. For Harvey ([1975] 2001: 247) capitalism is a contradictory totality whose "crowning glory" is the creation of a built environment to further accumulation. At the same time, this built environment is a "prison" that can stifle profit-making as inherited networks and infrastructures can impede market formation, and erect barriers and impediments to capital circulation. As a contingent process of socio-spatial restructuring, capitalist development thereby has to negotiate a "knife-edge path" between preserving the fixed social structures that underpinned and supported past capital investments and destroying these structures in order to create new opportunities for investment. As a consequence, according to Harvey, we "witness a perpetual struggle in which capitalism builds a physical landscape appropriate to its own condition at a particular moment in time, only to have to destroy it, usually in the course of a crisis, at a subsequent point in time" ([1975] 2001: 247). Thus, the built environment that capitalism creates is a locus of fragmentation, polarization, and perpetual upheaval.

My basic argument is that the housing finance sector is permeated by significant contradictions and irrationalities that reflect the disruptive and unstable financial process of transforming illiquid commodities into liquid resources. In the sections below, I argue that over the past several decades the process of "securitization" – for example, converting opaque and illiquid assets into liquid and transparent securities – has become a major crisis-management strategy to remedy the contradictions of capital investment and circulation via the housing finance sector.

Securitization is designed to reduce the uncertainty of buying and selling atypical assets (leases, homes, loans, etc.) by transforming them into marketing investments that have common features and characteristics. As a mechanism for easing the spreading and trading of risk, securitization has been a major financial innovation that has allowed private and public actors to finance local property development and housing in the national and international capital markets. As a process of financial globalization, securitization consists in large part of homogenizing diverse commodities and weakening the institutional buffers between local, national, and global markets. Before the 1980s, consumer loans like home mortgage loans, automobile loans, student loans, and credit card receivables had been held in commercial and savings bank portfolio. In the 1980s and later, securitization enabled lenders and banking institutions to repackage these relatively illiquid assets into standardized, transparent, and interest-bearing securities for resale in global securities markets.

New legislation, regulatory strategies, and public policies have promoted the development and integration of securities markets, the formation of large pools of private investment capital, and the development of new real estate financing tools – for example, adjustable rate mortgages (ARMs), mortgage-backed securities (MBS), real estate investment trusts (REITs), among others. The potential advantages of securitization include enhanced flows of funds across borders; greater distribution of risk to lenders most willing to bear it, which reduces price of risk; and increased availability of credit. As noted in Wainwright's chapter, securitization is not a static thing but a historical process that has undergone relentless innovations as it has spread, albeit unevenly, across the globe.

As I point out, the securitization of real estate is a process of creating liquidity out of spatial fixity that is characterized by complex struggles and contradictory interests that reflect and reinforce the crisis-prone nature of capital accumulation and circulation in the built environment. I conceptualize spatial fixity as a condition of non-exchangeability, non-transferability, immobility, illiquidity, and long turnover times between buying and selling. Spatial fixity also refers to a commodity that has diverse, idiosyncratic, and inconsistent properties such that it is difficult for buyers and sellers to know the value and property of what they are exchanging. A liquid asset or resource, in contrast, has homogeneous, predictable, and standardized features that enable financial actors to convert it into cash quickly and easily. Exchangeability and marketability define liquid commodities. Liquidity is neither a psychological phenomenon nor an immutable or durable feature of an asset. As a social construction, liquidity is variable, contingent, and dependent on state actions and legal and regulatory frameworks to support the standardization, homogenization, and exchangeability of commodities. State policies, regulations, and legal actions can impede or facilitate the development of market liquidity. More important, creating markets for liquid capital reflect the politics of liquidity, including political struggles and conflicts over the formulation and implementation of housing finance policies and other socio-legal regulations pertaining to mortgage markets and financing instruments.

As far as possible, securitization attempts to standardize and rationalize non-transparent and localized commodities (like mortgages) so that different buyers and sellers in different places around the globe can understand their features and qualities and exchange them easily.

The securitization of mortgages is driven by a deep tension between local social relations and networks of real estate activity that generate knowledge about a home and its distinctive characteristics, and the reach of markets to extract that knowledge, reduce its unpredictability, and routinize and commodify it. Yet the spread of securitization to mortgages and other commodities is not a one-way process, nor is it necessarily functional, rational,

or inevitable. Rather, securitization has developed as a result of substantial and ongoing legal and regulatory reforms that have been implemented on an ad hoc basis to remedy past economic crises. Such an account eschews a “capital logic” argument and examines the ways in which state policies and legal/regulatory actions to create and enhance the exchangeability of otherwise illiquid commodities are historically contingent, conflictual, and contradictory.

Past legal/regulatory actions have fed back into the US housing system by creating new financial flows, exacerbating uneven development, and destabilizing markets as recently revealed through the subprime mortgage crisis. Understanding the changing institutional linkages between housing finance, securitization, and state policy not only provides useful insights into the causes of the current financial crisis but also presents an opportunity for theoretical development into the sociology of mortgage markets. The conflicts over the securitization of illiquid assets – that is, the creation of liquidity out of spatial fixity – represent intense struggles over efforts to annihilate space through time within mortgage markets and the real estate sector more broadly.

I begin by describing the theoretical orientation that informs the analysis of the historical development and recent restructuring of the US housing finance system. I examine the rise of the New Deal system of housing finance and the growth of the savings and loan industry. I then describe the economic vulnerabilities of the savings and loan industry and the various policy reforms enacted during the 1960s through the 1980s to transform mortgages into liquid resources via the process of securitization. Next, I focus on two major regulatory drivers of the housing finance crisis: first, the expansion of private-label securitization and, second, the crucial role played by the US Treasury Department’s Office of the Comptroller of the Currency (OCC) in nurturing the growth of a market for securitizing subprime loans. My historical analysis suggests that state strategies to guide investment in real estate and transform illiquid commodities into liquid resources have developed over time in conjunction with past political circumstances and sociopolitical struggles.

As I point out, the state plays a key role in the dialectics of spatial fixity and liquidity through a variety of policies, legal-regulatory actions, and infrastructural investment that can enhance the exchangeability of mortgages, and contribute to and exacerbate crisis tendencies within the finance and real estate sectors. I draw on recent theorizations of the secondary circuit of capital to illustrate the ways in which securitization has been both a response to and cause of financial crises. Whereas securitization was a major regulatory response to the savings and loan crisis of the 1980s and 1990s, today we recognize securitization as an important cause of the subprime mortgage crisis that has spread globally to affect mortgage and

financial markets around the world. In conclusion, I suggest that we view recent state policies to mitigate the financial crisis as crisis management strategies designed to resolve the contradictions created by previous state-led interventions in the housing finance sector.

Real Estate, Housing, and the Secondary Circuit of Capital

My empirical interest in the housing finance system stems from a larger theoretical interest in understanding the links between recent regulatory reforms and structural changes within the “secondary” circuit of capital investment. Initial work by Henri Lefebvre (2003) and David Harvey (1978; 1985) drew attention to the use value and exchange value of real estate and the crucial distinction between the primary and secondary circuits of capital investment. The primary circuit involves capital moving in and out of manufacturing and industrial production, while the secondary circuit refers to capitalist investment in land, real estate, housing, and the built environment. Influenced by Karl Marx, Lefebvre and Harvey maintained that a central component of the overall dynamic of capitalist development lay in the production of the built environment and the process of city building. Both stressed the important influence of private and public financial structures in channeling capital into metropolitan development and the tendency towards crisis within the primary and secondary circuits. The secondary sector, according to Lefebvre, absorbs economic shocks that periodically affect capitalist societies. Harvey’s oft-cited thesis attributed the growth of postwar US suburbs to the switching of capital out of the primary circuit, where crises of over accumulation were emerging at mid-century, into the secondary circuit of real estate investment (Harvey 1975). In particular, Lefebvre and Harvey drew attention to several theoretical components that laid the groundwork for understanding the importance of land and real estate in the production of space: the relation of the built environment to the sphere of production, the role of capital accumulation in the built environment, the mediation of financial institutions, and the cyclical nature of capital investment in the primary and secondary circuits (for an overview, see Gottdiener 1994).

Over the decades, the theoretical richness of Lefebvre’s and Harvey’s arguments have inspired scholars to investigate capital flows into and out of the real estate sector, identify the crisis tendencies and contradictions of the secondary circuit, and fashion new theoretical and analytical tools to examine real estate processes and their linkages with uneven metropolitan development. Early work by Feagin (1982; 1987) attempted to confront Harvey’s thesis directly by examining the irrationality of accumulation and investment processes within the real estate sector. In her discussion of the

“relative autonomy” of the primary and secondary circuits, Haila (1998; 1991) pointed to the mobilization of particular organized interests – for example, developers, local governments, financial institutions, and real estate brokers, among others – who are concerned not only with investing in property for speculative objectives but also in generating new investment opportunities distinct from those in the primary circuit. Beauregard’s (1994) study of the 1980s building boom in the United States found little support for the capital switching thesis and, more important, pointed to the delinking of real estate investment from non-speculative investment criteria and use value considerations.

Recent research on the secondary circuit eschews a conception of real estate as a by-product or outgrowth of “industrial” capitalism and theorizes the real estate sector as having an intrinsic quality or *sui generis* character that forms an independent sector of the economy. Charney’s (2001) case study of the Canadian real estate sector draws attention to how real estate companies attempt to capitalize on segmented real estate markets by using “three dimensions of capital switching” within the secondary circuit. Real estate companies can switch between modes of operation, between property types, and between geographical areas (i.e., spatial switching). More recently, Aalbers’ (2007) examination of the Milan, Italy mortgage market suggests that capital switching does not necessarily reflect a post hoc response to economic crises per se. Capital switching can represent a proactive and consciously planned strategy taken by capital to exploit the lucrative opportunities that the built environment provides. Overall, the work of Charney, Aalbers, and others views the real estate sector as a conceptually separate and analytically distinct circuit of capital investment that is organized by diverse networks of actors, organizations, and laws and public policies (Gotham 2006; 2002). The secondary circuit is not the exclusive domain of separate real estate agents, but consists of a structure of banks, other financial conduits, and diverse modes of agency, such as monopolistic and small real estate and financial firms, appraisers, public and private investors, and homeowners (Feagin 1982; Gottdiener 1994: 185–94).

Conceptualizing and analyzing the dynamics of the secondary circuit suggests a theory of circulating capital that emphasizes the irrationalities of the circulation process and the systemic crises that periodically affect real estate markets. In Volume 3 of *Capital*, Marx (1991: 78) argued that capital creates institutional and financial structures and networks that can become sources of ruinous competition and obstacles to future investment: “The *true barrier* to capitalist production is *capital itself*,” Marx theorized. From this perspective, real estate’s time in circulation – that is, the period of time from the production of value to the realization of value in commodity exchange – can be both an opportunity and constraint to profitability.

Real estate can aid capital accumulation, if it is a profitable avenue for commercial investment and a source of mass consumption in the case of homeownership. Investment in real estate, housing, and land can be an important means of accumulating wealth and a crucial activity that pushes the growth of metropolitan areas in specific ways. Further, once built, residential real estate and housing provides access to other commodities; spatially embeds classes, races, and ethnic groups; and channels the spatial growth and movement of industrial capital.

Real estate can be a barrier to capital accumulation, however, when its enduring qualities render it outdated and anachronistic, or when financing needed to construct, sell, and rehabilitate it are unavailable. According to Gottdiener (1994: 191), investment in real estate generates bust-and-boom cycles of investment and “propels the never ending process of property turnover and spatial restructuring whether an area needs it or not.” This process of “creative-destruction,” of destruction and demolition, expropriation and rebuilding, and rapid and incessant changes in use as a result of real estate speculation and obsolescence are the most recognizable signs of uneven metropolitan development in the United States.

In short, the analysis of the secondary circuit of capital reveals a basic contradiction. On the one hand, real estate is by definition illiquid, spatially fixed and immobile, and defined by local particularities and idiosyncrasies. Geir Inge Orderud’s (2006) analysis of the Norway housing sector suggests that home building is “a local business due to: a capacity restraint regarding local market knowledge; the interaction with local planning authorities; face-to-face meetings; and social relations.” On the other hand, capital is abstract, nomadic, and placeless. Insofar as possible, capital seeks to eradicate local peculiarities and place distinctions that characterize the buying and selling of commodities and thereby eliminate the spatial barriers to the circulation of capital.

It is this duality, or inherent contradiction, between immobile properties and mobile capital that defines modern capitalist urbanization and uneven development. In Lefebvre’s (2003: 159, 212) account of capitalist growth during the twentieth century, investment in the secondary circuit has assumed a life of its own as

speculation henceforth becomes the principal source, the almost-exclusive arena of formation and realization of surplus value. Whereas the proportion of global surplus value amassed and realized in industry declines, the amount of surplus value created and realized in speculation and property construction increases. The secondary circuit thus supplants the primary circuit and perforce becomes essential.

Harvey (1985: 11) echoes this tendency in his assertion that urban growth has changed “from an expression of the needs of industrial producers

to an expression of the power of finance capital over the totality of the production process.”

Below, in my analysis of the historical development of the US housing finance sector, I show that creating liquidity out of spatial fixity is an uneven, multidirectional, and open-ended restructuring process that is frequently associated with crisis-generating breakdown and instability. Liquidity is both a social relation between buyers and sellers of risk, and a process of exercising financial power in and through certain political and institutional arrangements. While the logic of capital creates opportunities and obstructions for change, various actors and organized interests interpret and construct the rules of the game through politics, policies, laws, organizational procedures, and other regulatory strategies.

As I show with the savings and loan crisis of the 1980s and 1990s and the recent subprime mortgage crisis, the interpretations of and responses to accumulation crises create new openings and prospects for transformation as well as legitimating calls for new policies to extend and enhance existing institutional structures of liquidity. State policies and interventions ultimately create a “catch 22 loop” whereby “old” policies produce crises of liquidity that inevitably bring forth calls for “new” policies that, once implemented, create further contradictions and unforeseen crises, a situation that then generates a new round of calls for “reform,” as we currently see with the subprime mortgage crisis and its spread to global capital markets. In this sense, the politics of liquidity take place on an aggressively contested institutional landscape in which past socio-spatial inequalities and regulatory arrangements interact with current political conflicts and struggles to control investment and accumulation. The establishment of new governance structures, state policies, and socio-legal arrangements to promote liquidity then provide a political arena in and through which class fractions and other organized interests battle to dominate and exploit markets, and control the accumulation process.

The New Deal Housing Finance System and Rise of the Savings and Loan Industry

The financial reforms of the New Deal represented the beginnings of federal involvement in establishing and subsidizing a national real estate sector and mortgage system that would last through the 1980s (for overviews, see Florida 1986b; Florida and Feldman 1988). Before the 1930s, federal involvement in housing markets was limited to the creation of a Federal Land Bank system in 1916 and the construction of military housing during the First World War. The establishment of the Federal Home Loan Bank Act (FHLB) in 1932, the Home Owners’ Loan Act in 1933, and the Housing Act of 1934 represented the beginning of a multifaceted federal effort to rebuild the

nation's housing and lending industries that had collapsed during the Great Depression. The Hoover Administration's FHLB included the creation of long-term amortized mortgages with low interest rates, and federal subsidies to aid private home building efforts and reduce housing construction costs (Radford 1996: 46–53; Davies 1958: 174–5; President's Committee on Home Building and Home Ownership 1932: 24; US Senate 1933). In addition, the FHLB created a system of federal home loan banks that could supply housing credit, and provide guidance, standards, and regulation over the private lending industry to expedite the flow of mortgage funds. The 1933 Act established the Home Owners Loan Corporation (HOLC), which systematized appraisal methods throughout the nation by devising a neighborhood rating system to assess the creditworthiness of the housing it financed (Harriss 1951). From 1933 to 1935, the HOLC refinanced approximately 20 percent of all outstanding mortgages on single family homes in the nation. This percentage amounted to one million loans worth approximately \$3.1 billion. By 1935, the HOLC held 12 percent of the nation's outstanding residential mortgage debt, more than life insurance or commercial banks (Colton 2002: 4).

The Housing Act of 1934 provided for the establishment of a modern mortgage insurance system under which the newly created Federal Housing Administration (FHA) would provide insurance to private lenders to protect them against loss on home rehabilitation loans and mortgages for new homes (US House 1934a: 1). In addition to insuring home mortgages, the FHA created national mortgage associations to buy and sell FHA-insured mortgages in an effort to make mortgage insurance available on a nationwide scale and maintain a continuous and geographically even circulation of funds in times of short credit. Continuing a trend begun by the HOLC, the FHA required that all government-insured loans be long term, fixed rate, have high loan-to-value ratios, and be fully amortized with low down payments (10 percent or less of the total housing cost). The FHA also required all government-insured mortgages to conform to specific regulations pertaining to minimum property standards and inspections, design of the structure, quality of building materials and construction, appraisal procedures, condition and location of site, and subdivision planning. The effect of this new mortgage system was to standardize and systematize mortgage lending practices throughout the nation and transfer the risk of mortgage investment from the private sector to the federal government (US House 1934b). In addition, the 1934 Act established the Federal Savings and Loan Insurance Corporation (FSLIC) to insure the accounts of federal savings and loan (S&L) associations (Federal Housing Administration 1959). The significance of the 1934 Housing Act was that it represented the first concerted and large-scale federal intervention into the housing market to stimulate consumer demand and prime the private sector to increase housing supply.

Title III of the Housing Act of 1934 provided for the incorporation of private national mortgage associations to create a secondary mortgage market to provide greater mortgage market liquidity and enhance the financing of housing and real estate. In the “primary” mortgage market, borrowers obtain loans from mortgage originators. In the “secondary” mortgage market, mortgage originators and investors buy and sell mortgages as bonds or securities collateralized by the value of mortgage loans. Enhancing the liquidity of residential real estate proved difficult in the first few years as the lack of a central institution and socio-legal infrastructure mitigated against the transformation of mortgages into liquid resources. In 1938, the FHA chartered the National Mortgage Association of Washington, renamed the Federal National Mortgage Associate (FNMA), nicknamed Fannie Mae, to buy and sell mortgages as an expedient to pumping capital into the residential construction industry. A related purpose of Fannie Mae was to stimulate cash flow to enable mortgage banks, savings and loan associations, and commercial banks to make new loans. During the first decade of its existence, Fannie Mae purchased 66,947 FHA-insured mortgages and sold 49,048. In 1949, Fannie Mae expanded its activities to include buying and selling mortgages guaranteed by the Veterans Administration (VA). During these years, the volume of VA mortgages purchased by Fannie Mae skyrocketed, going from 6734 mortgages in 1948 to 133,032 mortgages two years later in 1950 (FNMA 1975).

Other New Deal reforms including the Glass-Steagall Act of 1933, the Securities and Exchange Act, and the Banking Act of 1935 erected rigid regulatory barriers between the various segments of the commercial banking and housing finance industries. Under the Glass-Steagall Act, Congress completely separated commercial banking and insurance, and prohibited banks from interstate operations and from offering insurance or securities. The Banking Act of 1935 created the Federal Deposit Insurance Corporation (FDIC) to protect depositors at FDIC-insured institutions and provide a means for insuring small depositors against losses arising from bank failure. The legislation also allowed the FDIC to review operations of those banks under its jurisdiction; issue regulations to promote safe and sound banking practices; and cancel insurance for banks engaged in unsafe and unlawful banking practices.

Through this New Deal housing system, housing finance became insulated from the national financial system. Highly localized and small savings and loans became the source of capital for housing finance while Congress designed the FHA to provide housing credit on a long-term basis. The savings and loan (S&L) or “thrift” industry, as it emerged after the 1930s, became the chief source of mortgages as the federal government protected the emerging industry from more volatile flows of funds in national capital markets by shielding savings deposits.¹ With financing from deposits, S&Ls

made conventional fixed, long-term loans to home buyers. Federal and state regulations limited the spatial investment reach of these lenders, restricting interstate banking activities and mandating thrifts to make mortgages in small local areas – within 50 miles of the home office until 1964, and within 100 miles after. From 1950 to 1977, the percentage of residential mortgage debt outstanding held by savings and loan associations increased from 36 percent to 65 percent (Colton 2002: 9). In subsequent decades, life insurance companies and commercial banks saw their share of the market for residential mortgage debt decline while the thrift industry grew at an astonishing rate, doubling their assets every five years and increasing their market share from less than one-fifth to almost one-half of all savings deposits (Hendershott and Villani 1977). By the mid-1950s, a system of specialized mortgage finance institutions had become a “second banking system” (Florida 1986a: 52), controlling a huge pool of resources and functioning under the jurisdiction of the federal government.

New Deal housing policies transformed the home building and loan lending industries by promoting economies of scale through suburban housing construction, a development related to federal efforts to promote the concentration of capital (home builders). The FHA’s home building subsidies, underwriting standards, and land-planning policies encouraged large builders to expand the scope of operations and market share by enhancing the financial feasibility of single-family homes. Community developers and large builders whose housing plans conformed to FHA standards were able to get a government-insured mortgage for all homes they built (Weiss 1987). Once the FHA subsidy was obtained, builders rapidly increased the size of their operations, producing a high volume of quality, moderately priced dwellings in suburban areas. In 1938, large builders accounted for five percent of all new housing starts. This figure increased to 24 percent in 1949 and 64 percent by 1959. Builders who could promise a large quantity of mortgages and new homes were the principal beneficiaries of federal housing subsidies while smaller builders were driven from the market due to their small-scale operations. For large builders, the FHA offered billions of dollars of credit and insured loans up to 95 percent of the value of the house. In Long Island, NY, the William Levitt and Son Company was able to get FHA subsidies to finance 4000 houses before clearing the land to build Levittown (Checkoway 1984:158–9). Overall, the level of housing production rose significantly after the Second World War, from 209,000 units in 1945, to more than a million units by the end of the decade, to as high as 2,379,000 units by the early 1970s. On an annual basis, production levels during the 1950s, 1960s, and the early 1970s were equally impressive, remaining above seven dwelling units per 1000 population during these years, reaching a peak of 11.4 in 1972 (Rowe 1995: 184). Overall, New Deal housing policies and tax provisions allowing homeowners to deduct mortgage interest and property

tax payments from taxable income fueled rises in homeownership, from 48 percent to 63 percent of all households between 1930 and 1970.

Economic Crisis and the Decline of the Savings and Loan Industry

Sharp swings in interest rates, changes in the availability of funds, and unstable production cycles characterized the New Deal housing system during the 1950s and 1960s, leading to calls for major reforms in governing regulations pertaining to housing (Guttentag 1961). Between 1962 and 1969, rising interest rates and plummeting housing starts prompted the Federal Home Loan Bank Board (FHLBB) to authorize a study into the vulnerability of the S&Ls to economic downturns and to recommend changes in the system of housing finance (President's Committee on Federal Credit Programs 1963). This FHLBB study, directed by Irwin Friend, recommended that the federal government promote economies of scale within the S&L industry, encourage industry consolidation through mergers and acquisitions, and develop new mortgage instruments such as gradual payment mortgages and variable-rate mortgages (Friend 1969). New savings inflows to S&Ls plummeted from \$8.4 million in 1965 to just \$3.6 million in 1966. Through the middle to late 1960s, residential construction declined dramatically experiencing a 23 percent decline between the first quarter of 1966 and the first quarter of 1967. This liquidity crisis prompted Fannie Mae to escalate its mortgage financing activities, purchasing \$2 billion in mortgages in an effort to stabilize the housing market (Green and Wachter 2005). By this time, political and economic elites recognized that a fundamental problem facing housing finance was the "maturity mismatch" between long-term mortgage credit and the short-term deposits that banks used to finance mortgages.

Relying on short-term deposits to fund long-term mortgages exposed the Achilles heel of the New Deal housing system and, in the context of the residential construction crisis of the 1960s, aggravated liquidity problems. In response, the federal government passed the Housing Act of 1968, which, among other policy innovations, removed Fannie Mae from the federal budget and privatized the agency as a shareholder-owned company. The legislation also created the Government National Mortgage Association (Ginnie Mae) to assume the management functions of Fannie Mae and guarantee FHA and VA mortgages. Two years later, the federal government created the Federal Loan Mortgage Company, or Freddie Mac, to compete with Fannie Mae in attracting investors to finance housing through an expanded secondary mortgage market. Legislation passed in 1968 and 1970 authorized Fannie Mae, Freddie Mac, and Ginnie Mae to issue securitized bonds to sell to private companies and institutional investors, and

represented a bold experiment to attract investment funds to the field of mortgage investment.

To ease the spread and trading of risk via mortgages, federal officials offered a “double guarantee” to create a liquid security, the mortgage pass-through security, that diverse buyers and sellers could understand and exchange. First, pools of securities would contain mortgages insured by the FHA or the VA to protect the investor if the homeowner defaulted. Second, these pools would protect investors if a bank that issued the securitized bonds defaulted. By decoupling risks from profits, the federal government during the 1970s was involved in developing a new housing finance tool, the mortgage-backed security, to promote investment in housing and enhance the marketability or liquidity of mortgages.

The turbulent recessions of 1969–70 and 1974–75, the oil crisis of 1973–74, and the collapse of the Bretton Woods system of fixed exchange rate destabilized the New Deal housing finance system and spurred legislators to enact sweeping reforms to remedy the spreading liquidity crisis. In 1979, the Federal Reserve implemented new regulations to restrict the growth of money supply, a development that caused interest rates to skyrocket. Between June 1979 and March 1980, short-term interest rates rose by more than six percentage points, from 9.06 percent to 15.2 percent. Borrowing at high interest rates to carry mortgages at lower rates caused Fannie Mae to lose millions of dollars and had contagion effects within the broader credit and financial markets.

To remedy the housing finance crisis, in the early 1980s, the US Congress passed the Depository Institutions Deregulation and Monetary Control Act (DIDMCA) of 1980 and the Garn-St. Germain Depository Institutions Act of 1982 that eliminated deposit rate ceilings, enabled S&Ls to invest in commercial banking, and allowed S&Ls to offer competitive money market type accounts. Also in 1982, Congress passed the Alternative Mortgage Transactions Parity Act (AMTPA), which preempted state laws to allow banks throughout the nation to use variable rate terms and balloon payments. These statutes also allowed S&Ls to offer adjustable interest rate mortgages (ARMs) to unload some of the credit risk onto consumers and help mortgage lending institutions match investment returns with interest expenses (see Chapter 8).

Rather than remedy the problems of the S&Ls, however, the regulatory initiatives passed in the 1980s destabilized markets and contributed to the demise of the thrift industry. New legislation and regulations raised interest rates on deposits, reduced rates on old mortgages, and allowed S&Ls to invest heavily in real estate speculation and the junk bond market. The relaxing of regulations and the rise of speculative financing caused catastrophic bank failures and eroded the multi-decade market dominance of S&Ls as suppliers of mortgage credit. In 1981 and 1982 combined, the S&L

industry reported almost \$9 billion in losses. On average during 1982–84, one S&L and one commercial bank failed every week. In 1983, the FDIC's list of problem banks grew by 25 institutions per month. Within a year, the rate of bank failures was increasing by three banks a week with the size of receivership assets owned by the FDIC at \$10 billion (Kane 1985: 2–3). Overall, bank failures increased from only 22 in 1980, 99 in 1983, 180 in 1985, 262 in 1987, 470 in 1988, and 534 in 1989.² From the 1930s through the 1970s, S&Ls provided nearly three-quarters of all new mortgage originations. By the early 1980s, this had declined to just one-fifth of new residential credit (Florida 1986a; 1986b). In short, the elimination of rate ceilings, the development of the adjustable rate mortgage and other loan instruments, and a lessening of legal restrictions that expanded the geographical areas in which individual banks could operate all worked together to inject a new form of competition into the housing sector that undermined the economic power of S&Ls and destabilized the New Deal housing system.

Securitization as Crisis Management Strategy

The savings and loan crisis of the 1980s and early 1990s caused major disruptions in the flow of mortgage capital and mobilized political and economic elites to pass legislation to increase the liquidity of mortgages through securitization and encourage the growth of the secondary mortgage market. Federal officials viewed the S&L crisis as a housing finance problem caused by the dominance of deposit-taking portfolio lenders in the mortgage market. Relying on savings deposits for mortgage loans limited the volume of loans S&Ls could originate. As noted by Baily, Litan, and Johnson (2008: 22), “securitization was seen as a solution to the problems with the S&L model, as it freed mortgage lenders from the liquidity constraint of their balance sheets.”

Federal statutes passed during the 1980s to expand the secondary mortgage market aimed to allow S&Ls and other lenders to sell mortgages to a third-party, take them off their books, and use the money from the sale to generate more loans for homeowners (for overviews, see MacDonald 1995; 1996). In 1984, Congress passed the Secondary Mortgage Market Enhancement Act (SMMEA) that removed statutory restrictions on investments in private MBSs by federal chartered depository institutions. Congress designed this legislation to expand the secondary mortgage market to increase the supply of funds available to mortgage borrowers, transform mortgages into liquid financial instruments, and facilitate the trading of mortgages. The Tax Reform Act of 1986 authorized Real Estate Mortgage Investment Conduits (REMICs), a financial tool that separated groups of mortgages (i.e., mortgage pools) into different risk classes as well as different maturity

classes, thereby insulating the financial performance of securities issued from the financial position of the issuer. A year later, Fannie Mae began using REMICs to attract investors not traditionally interested in mortgage-related investments.

The Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) established the Resolution Trust Corporation (RTC) to liquidate the assets of hundreds of failed banks and moved S&L regulatory authority from the Federal Home Loan Bank Board to the Office of Thrift Supervision (OTS) (US House of Representatives 1989a; 1989b). One of the primary goals of the FIRREA, and later amendments, was to bolster the supply of mortgage credit by requiring S&Ls to sell mortgages held in portfolio to the secondary mortgage market. The FIRREA also created a board of directors to supervise Freddie Mac and appointed HUD as the major oversight body of the GSE. The supervisory and regulatory structure of the FIRREA was further rationalized through the Federal Housing Enterprises Financial Safety and Soundness Act (FHEFSSA) of 1992. This legislation created the Office of Federal Housing Enterprise Oversight (OFHEO) as a new regulatory office within HUD with the responsibility to “ensure that Fannie Mae and Freddie Mac are adequately capitalized and operating safely.”³ The FHEFSSA established risk-based and minimum capital standards for Fannie Mae and Freddie Mac, and established HUD-imposed housing goals for the financing of affordable housing. Overall, the passage of legislation and the establishment of federal policies and regulations helped define a legal infrastructure for regulating market transactions and enforcing contractual relations to expand the secondary mortgage market.

By the beginning of the millennium, institutional conditions were in place to enhance the liquidity of mortgages thereby providing incentives to domestic and foreign investors to invest capital in residential real estate (Gotham 2006). By this time, securitization had become the primary vehicle for financing the buying and selling of mortgages in the United States. Over the last two decades, the creation and institutionalization of new financial instruments such as the MBS, structured investment vehicles (SIV), the collateral mortgage obligation (CMO), the collateral debt obligation (CDO), and others have uprooted or disembedded the financing of real estate from local networks of accumulation and enmeshed real estate financing within global capital markets. Unlike the MBS that permits the bundling homogeneous risks in the securitization process, SIVs combine many forms of debt and risk to sell to different investors. CMOs are a more complex and sophisticated variation of the MBS that differs in the temporal structure of the expected payments. With a CMO or a CDO (collateralized debt obligation), payments are divided into tranches, with the first one receiving the first set of payments and the later ones taking their turn. CDOs and CMOs

are assets and bonds that represent pools of MBSs and other securities that banks and lenders have collected and resecuritized.

As resecuritized securities, CDOs are intended to further diversify investor risk. Mortgage companies and financial institutions can structure CDOs in a variety of ways and can include complex “multi-tranche” structures that complicate refinancing and expose different investors to different degrees of risk. CDOs can be securitizations or re-securitizations of commercial loans, corporate bonds, other types of residential MBSs, commercial MBSs, and debt. The development of structured securities such as the MBS, CMO, and CDO is a process of enhancing the liquidity and exchangeability of mortgages by dividing and subdividing the cash flows into separate “strips” or “tranches” with different yields, maturities, and credit quality and risks (for overviews, see Chapters 4 and 8; Green and Wachter 2005).

We can view the “tranching process” of dividing and subdividing securities, securitizing and re-securitizing securities ad infinitum, and creating multi-tranche securities as a complex and unpredictable process of commodity rationalization, differentiation, and fragmentation. SIVs, CMOs, CDOs, and so on, transform risk in unique ways by generating exposures to different “slices” or tranches of the securitized mortgage, a process that is designed to distribute risk to different parties and thereby improve the trading of different assets. The assumption underlying securitization and tranching is that the partitioning of a commodity into separate securities can enhance the liquidity, or exchange-value of the overall mortgage. Yet mortgages have maturities that are non-standardized, unpredictable, and uncertain. As illiquid commodities, mortgages require messy maintenance and labor-intensive upkeep to assess risk and maintain their value. Collecting monthly payments, making sure real estate taxes are paid, keeping track of slow-pay and no-pay borrowers, and sending out annual statements of interest and taxes paid all require a costly infrastructure of institutions and networks of organizations. Thus, the development of securitization and other financial tools to transform illiquid assets into liquid securities – for example, MBSs, CDOs, CMOs, and so on – represent attempts by economic actors and financial institutions to minimize and eliminate the obscurity and opacity of the mortgage commodity and enhance their exchangeability.

In short, the expansion of securitization has been a major crisis management strategy to address the crisis of accumulation within the S&L industry. As a mechanism for responding to the problem of under consumption within the housing finance sector, securitization expresses the relentless formation and reformation of financial instruments to extend purchasing power and mitigate the omnipresent threat of devalorization. As the subprime mortgage crisis illustrates, however, the process of securitization has introduced new problems and contradictions that are destabilizing markets, reinforcing inequalities, and perpetuating patterns of uneven development.

The Subprime Mortgage Crisis and the Role of the US Federal Government

One popular view shared by many journalists and researchers is that the subprime mortgage crisis can be explained with reference to “deregulation” or lax regulation by federal and state agencies.⁴ Immergluck’s (2009) account of the rise of subprime mortgage lending argues that financial innovations, deregulation, and failure of regulators to maintain control over new mortgage products facilitated excessive risk taking that harmed different populations and communities. The deregulatory fervor that marked the passage of legislation during the 1980s later lessened the constraints to buying and selling mortgages in the secondary mortgage market and facilitated a vast expansion of credit (see Chapter 3). Securitization is an outgrowth of various deregulation measures that have broken down the institutional and legal barriers to international exchange and encouraged the buying and selling of risk. Deregulation does not mean withdrawal of the state from regulating society. Nor does this term suggest or signify a reduction or diminution of state power and authority. Rather, deregulation is a conscious policy decision that reflects an application of state power to transform property rights and rules of exchange to enable actors in markets to engage in profitable exchange.

In addition to focusing on the significance of deregulation and failure to regulate, it is also important to direct attention to the ways in which different state institutions and agencies formulate and implement various policies, statutes, and legal-regulatory frameworks to encourage and facilitate subprime lending. As Aalbers notes in his introduction, “no state regulation, no property rights, no mortgage market.” As we have seen, state activity has always been involved in the deregulation and reregulation of mortgage markets and state policies have been critical to the financialization of the economy. The state promoted the growth of the New Deal housing system that enabled suburban development, deregulated the S&L industry causing catastrophic results, and reregulated the mortgage market through the development of the MBS and other structured finance tools that created new incentives for risk-averse and high-risk investors. By increasing the demand for, and supply of, mortgage capital, according to Newman, “national housing, macroeconomic and tax policies have expanded the importance of banking and finance within the global and national economy” (2009: 314; see also McCoy and Renault 2008). In short, deregulation and reregulation have combined and worked in tandem to encourage the subprime mortgage crisis. The erosion of lending standards and the dismantling of socio-legal regulations to protect consumers have interacted with the new legislation to fuel the rise of exploitation and speculative lending practices.

Before the mid 1990s, the vast majority of mortgages bundled into securities were traditional prime loans that lenders sold to consumers who could

prove they were affluent enough to buy homes. Beginning in the late 1990s, however, lenders began bundling “subprime mortgages” into private-label MBS that did not have the federal government’s backing. To create a market for their products, many lenders engaged in a variety of deceptive and “predatory” lending practices to sell mortgages to borrowers with poor credit. Some were misrepresenting the terms of loans, giving huge loans to people who could not repay, creating loans with deceptive “teaser” rates that later ballooned, packing loans with undisclosed charges and fees, or even paying illegal kickbacks (see Chapter 8). In one publicized case, EMC Mortgage, a subsidiary of Bear Stearns, serviced hundreds of thousands of subprime mortgages and hit customers with unauthorized fees, misrepresented how much money homeowners owed, harassed consumers with property inspections, neglected to keep track of loan balances, escrows, and payment histories, and failed to tell national credit report bureaus that borrowers were disputing false reports.⁵ To combat the surge in predatory lending, several state legislatures passed anti-predatory legislation. In 1999, the state of New York sued Delta Funding Corporation for predatory lending. In 2002, attorneys general from all 50 states entered into a settlement with Household Finance that resulted in restitution of \$484 million to victims of predatory lending. In 2006, attorneys general and banking regulators in 49 states settled a \$325 million lawsuit with Ameriquest Mortgage Company for engaging in predatory lending practices. During these years, state legislatures in North Carolina (1999), Georgia (2002), and New York (2003) passed anti-predatory lending laws to curb exploitative banking practices.⁶

National banks and their lending subsidiaries bitterly fought these new state regulations and embarked on an aggressive campaign to prevent state governments from passing and enforcing laws to halt predatory lending practices. In 2001, the U. Treasury Department’s Office of the Comptroller of the Currency (OCC) ruled that banks’ “operating subsidiaries” should not be subject to state control. Two years later, the OCC issued a series of formal opinions and new rules that negated all state predatory lending laws, thereby rendering them unenforceable. With state laws nullified, national banks and their state subsidiaries could engage in a variety of exploitative lending practices that states had hoped to stamp out. In response, all 50 state attorneys general, and all 50 state banking superintendents, actively fought the new rules and launched suits against the OCC. The national banks and their allies maintained that an unduly burdensome patchwork of state rules and regulations was stifling profits and denying access to credit for consumers. The states argued that their role was lawful and necessary to protect consumers from predatory lending practices and other potential violations. In the end, in 2007, the US Supreme Court ruled in a five to three decision that states could not regulate the mortgage-lending subsidiaries of national banks.⁷ By this time, however, the OCC had successfully created the

legal conditions to encourage predatory lending and permit the aggressive mass marketing of unaffordable and exploitative mortgage products to vulnerable consumers.

From the late 1990s through 2005, rising housing prices contributed to a liquid mortgage market characterized by low loan default rates, increasing homeownership, and escalating subprime lending. A major vulnerability of subprime lending was the optimistic assumption that home values and prices would increase indefinitely (Immergluck 2008). Nationally, average housing prices peaked in the second quarter of 2006 and entered into a period of decline. Once housing prices stopped rising, subprime borrowers could not refinance their homes to pay off their loans before they adjusted to higher and unaffordable interest rates; a condition that produced a vast supply of foreclosed, vacant, and unsold homes. By 2008, the United States was facing huge increases in loan delinquencies and housing foreclosures, a perilous situation that has contributed to widespread bank losses, and declining tax revenues and major budget deficits for local and state governments.⁸ The crisis in home lending reached a major milestone in March 2008 with a report from the Mortgage Bankers Association (MBA) finding that 2.04 percent of outstanding mortgages were in foreclosure in the fourth quarter of 2007; an all time high. The announcement came shortly after a Federal Reserve study showing that the ratio of owner equity to debt in US homes fell below 50 percent in 2007, a first since 1945.⁹ Today, we witness a crisis of overaccumulation and devaluation in the financial and real estate markets, in which the consumers cannot afford homes to own or rent and banks and mortgage companies have reduced their lending in times of uncertainty.

Discussion

The above points resonate with Harvey's famous thesis in the *Limits to Capital* (1999: 83) that capital "as value in motion" is always under the threat of devaluation through decelerated turnover time. Production and realization of profits through real estate takes time: entrepreneurs and firms have to invest capital prior to the production of the built environment, and they can only realize profits after the completion of production and the selling of the spatially fixed commodity. Thus, there is always a time lag between investment and payoffs in real estate. On the one hand, the long turnover time of real estate can provide an attractive linchpin for capital at times when the average rate of profit is low, due to its long amortization, diverse use values, and heterogeneous markets. On the other hand, the long turnover time of real estate increases its risk due to the unpredictability and uncertainty of the economic and political environment. As capital immobilized in space, real estate always faces intersecting and multiple crises of realization, repayment,

and falling rates of profit. To solve this contradiction, the state must liberate capital from its spatial fixity, reduce the uncertainty and unpredictability of exchange, raise the rate of profit to make room for new investments, and promote flows between territories. As a mechanism for extracting and stripping wealth from the homeowner, subprime mortgages – especially so-called exotic mortgages with interest-only payments, negative amortization, and adjustable rates – are tools of exploitation that reflect a long history of attempts by banking and financial institutions to increase profits, mitigate omnipresent crises of accumulation, and exploit markets.

Transforming mortgages and other long-term debt into liquid securities is an attempt to bring greater rationalization, standardization, and exchangeability to the difficult and conflictual process of buying and selling complex commodities that have a variety of use values and exchange values. The major contradiction is that these financial tools reflect and reinforce the cyclical dynamics of overaccumulation and devalorization that are *sine qua non* of capitalism. In the New Deal housing system, S&Ls originated mortgage loans and financed housing through savings deposits of customers, a process that concentrated risk within the lending agencies and limited the volume loans they could finance. At the same time, this localized system of mortgage finance reduced information asymmetries between the originator of the loan and the lenders who held the underlying risk, a system that encouraged sound risk analysis. As noted by Immergluck (2008), by holding the loans for up to 30 years, the S&L originators had a financial incentive to monitor their quality, investigate whether borrowers could repay the mortgage, avoid high risk lending, and invest in gathering information about borrowers and communities. In contrast, the securitization of mortgages creates and exacerbates information asymmetries between originators of the mortgage and investors, as the former have little financial or reputational incentive to engage in rigorous and thorough risk analysis since the loans will eventually be sold to a third party within the secondary mortgage market.

With the development and expansion of securitization, the various steps in the origination, servicing, and investing in mortgages were unbundled and broken up into differentiated and autonomous steps controlled and managed by different institutional actors. In the securitized system, brokers process mortgage applications, lenders originate the loans, large mortgage banking organizations purchase the loans and aggregate them into pools, investment banking firms issue securities based on these pools, and investors from around the world purchase the securities. Unlike the primary mortgage market where the source of profit is the payment of the mortgage to the bank that originated the home loan, the source of profit in the secondary market for securitized mortgages is the sale of mortgage pools that contain hundreds or thousands of individual mortgages. It is interesting, as Sassen notes in Chapter 3, that it is not the creditworthiness of the homebuyer that

is important in this securitized system, but the opportunity and capacity to maximize profits through the global circulation of the pooled mortgages.

As we have seen with predatory lending and the subprime mortgage crisis, securitization has created new windows of opportunity for financial actors to engage in speculative and exploitative financial activities, displace risks onto vulnerable groups, and evade accountability. Not surprisingly, a variety of studies, including the chapters by Hernandez, Sassen, Newman, Wyly, *et al.*, and Dymski in this volume, show that racial and ethnic minorities are more likely than Whites to get subprime mortgages and, therefore, bear the brunt of negative consequences of subprime-induced mortgage market downturns and financial crises (see also Squires 2004; Bond and Williams 2007; Williams, Nesiba, and McConnell 2005; Squires, Hyra, and Remer 2009). In their study of the racial distribution of subprime mortgages, Calem, Gillen, and Wachter (2004) found that, even after controlling for a variety of socio-economic factors and other characteristics, all-Black census tracts had a share of subprime mortgages that was 24 percentage points higher than an otherwise equivalent White census tract. In July 2007, the National Association for the Advancement of Colored People (NAACP) filed a discrimination suit against 11 of the largest lenders in the United States, arguing that racial minorities are steered toward subprime loans more than Whites, even after controlling for all risk factors.¹⁰

The above points suggest that securitization is an inequality-reinforcing process that reflects and reinforces the historically contradictory dynamics of capitalist investment in the built environment. As we have seen, securitization is associated with a series of regulatory dilemmas. On the one hand, securitization can serve as a basis for the accumulation process as mortgages and other illiquid commodities are transformed into liquid assets. On the other hand, securitization can operate as a barrier to accumulation as different state policies and regulatory strategies undermine previously stable patterns and networks of exchange and social reproduction. For this reason, and as we have seen with the historical development of the US housing finance system, securitization has not only helped create new opportunities for capital investment and growth but has also introduced new instabilities that are destabilizing mortgage markets and national economies around the world. Today, as the subprime mortgage crisis morphs into a global financial crisis, political and economic elites have become embroiled in a controversial politics of liquidity in which pressures to discard and rework extant institutional frameworks and regulatory strategies has become particularly intense. We now find ourselves in a period of institutional searching and regulatory experimentation in which diverse actors, organizations, and political alliances are promoting a variety of competing financial models and policies. Thus, the current politics of liquidity reflects the politically contested interaction between past institutional forms and policy frameworks

that underpinned the securitization process and emergent strategies of state policy and regulation that seek to remedy the problems and crisis tendencies of securitization.

Conclusions

The subprime mortgage crisis has exposed the inability of securitization to address the long running problems of uneven development and endemic financial crisis that affect capitalist economies. Over the last few years, the subprime crisis has mushroomed into a worldwide financial crisis. Vast quantities of capital are being devalued as financial firms cannibalize and liquidate each other in a battle to undermine competition and dominate mortgage markets. We cannot deduce the specific regulatory arrangements and policy outcomes in advance because they are the product of inter- and intra-class conflicts over the formulation and implementation of state policy. Today, the combination of increasing concern with exploitative loan practices, housing foreclosures, bank failures, and persistent housing affordability problems are igniting a new round of regulatory battles over housing finance. In 2008, the Federal Reserve proposed new rules to curtail abuses in mortgage lending, including barring lenders from penalizing subprime borrowers who pay their loans off early, forcing lenders to make sure that subprime borrowers set aside money to pay taxes and insurance, restricting loans that do not require proof of a borrower's income.¹¹ Mortgage industry officials, on the other hand, have bitterly fought these rules and proposed alternative plans and policies. Thus, current battles pit housing activists and advocates for victims of subprime and predatory lending against powerful corporate banking interests bent on shaping new regulations to promote free markets and entrepreneurialism. Speculative investments, untraceable financial schemes, and complex international financial networks make up this entrepreneurialism and, when combined with an increasingly global investment environment and deregulated system, exacerbate the potential for an even deeper crisis in housing finance than that which we have seen in recent years.

Overall, the development of the MBS, CDO, CMO, and other structured finance instruments underscores capital's relentless drive to annihilate space by time, to increase the liquidity of illiquid assets like mortgages. As active participants in promoting new financial innovations, banks and financial institutions have created new liquidity enhancement tools to reduce the turnover time of capital by increasing the fluidity and velocity of market transactions. In buying the original mortgages and then buying the tranches for the CDOs, powerful banks and lending institutions could leverage diverse kinds of investments and profit enormously. Financial giants

such as Bear Stearns, Lehman Brothers, J.P. Morgan, Merrill Lynch, and other lending institutions originated, packaged, and sold subprime mortgages to diverse buyers including British hedge funds, German savings banks, oil-rich Norwegian villages, and Florida pension funds, among others. While securitization and the tranching process multiplied investors' options and flexibility, they offered only a short-term temporal fix to the crisis-prone nature of capitalism. The negative consequences of securitization include greater instability in the mortgage market, greater speculative investment, and increased levels of indebtedness. In the United States, the rise and fall of the subprime mortgage market has followed a conventional boom–bust lending trajectory, in which intense growth and profit-making leads to market paralysis, financial sector imbalances, and accelerating inequalities. Fears over MBSs, CDOs, and CMOs, are raising doubts about the resilience and robustness of mortgage markets and fueling a contagion effect, with investors now shy of a wide range of securitized products. Thus, the subprime mortgage crisis is instructive in the impact of state laws and financial regulations in exacerbating the economic problems that they were supposed to remedy.

The empirical analysis and theoretical arguments I have laid out in this chapter provide a challenge to accounts that maintain that mortgage finance policy and securitization strategies have been successful in promoting efficient markets and optimal economic development. Mainstream economics assumes the existence of market equilibrium, harmony, and optimization; promotes the idea that market forces of supply and demand promote efficiency and overall social betterment; and views land use and metropolitan development as resulting from the operations of a self-regulating “free market” that is unfettered by the actions of power groups or elites.¹² Yet, the subprime mortgage crisis suggests that disequilibrium, instability, and cycles of boom and bust (overaccumulation and devalorization) are more valid for explaining the dramatic and chaotic transformations that are affecting cities and metropolitan areas. In contrast to mainstream work in economics, which has sought to discover the stable and progressive aspects of capitalism, the account I have offered here exposes the limits and contradictions of the securitization process. Thus, the subprime mortgage crisis reveals the intense destructive power that lurks behind the facade of societal progress and economic affluence. Just as capital continually renders obsolete and irrelevant the built environment and socio-spatial structures it creates, capital continually mobilizes new territories and spaces as sources of investment and profit. In this sense, the creation and destruction of mortgage markets and financing tools are premised upon the “production of space” (Lefebvre [1974] 1991).

Finally, my conceptualization of securitization as a process of creating liquidity out of spatial fixity dovetails with theoretization that emphasizes

the conflictual, contested, and deeply contradictory nature of uneven geographical development. Many scholars have noted that uneven development is endemic to capitalism and represents a key expression of capital's insatiable drive to mobilize spaces, places, and territories as forces of production (Harvey 1985; Brenner and Theodore 2002; Smith 1984). Uneven development is both a medium of intercapitalist competition and class struggle, and an evolving socio-spatial organization through which the process of securitization has unfolded. At the same time, securitization is permeated by tensions, antagonisms, and conflicts that are destabilizing the process of capital accumulation and circulation within the real estate sector. Just as capitalist regulation and profit-making occur as systems of rules, habits, and norms that constrain action, securitization is a set of socio-legal relations that define mortgages and tranches as standardized and exchangeable commodities (securities). As a result, securitization has developed through the production of historically specific patterns of socio-spatial organization, uneven development, and legal-regulatory policy. Today, the profitability and efficacy of securitization is being questioned as the specter of devalorization rattles financial markets, and financial firms and banks raise doubts about the long-term resilience and robustness of market liquidity. Thus, securitization has become contested terrain, a political arena in and through which struggles over the regulation of housing finance and real estate, and their associated contradictions, are being articulated and fought out both domestically and internationally.

Notes

- 1 I use "thrifts" and "savings and loans" interchangeably to refer to federally insured savings institutions that have traditionally provided home mortgage loans.
- 2 See Federal Deposit Insurance Corporation (FDIC). Historical Statistics on Banking; Bank and Thrift Failure Reports. <http://www2.fdic.gov/hsob/SelectRpt.asp?EntryTyp=30> (accessed January 15, 2008).
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- 5 Harney, K.R. September 20, 2008. "Settlement Sheds Light on Boom's Bad Practices." *Washington Post*. P. F1.
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- 7 Barnes, R. and El Boghdady, D. April 18, 2007. "High Court Sides With Banks on Mortgage Rules States Can't Regulate Loan Subsidiaries." *Washington Post*, p. D01.
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- 11 Aversa, J. July 13, 2008. "Fed Poised to Curb Shady Home-Lending Practices." *USA Today*. http://www.usatoday.com/news/washington/2008-07-13-2483477143_x.htm (accessed October 25, 2008).
- 12 See Dymski's chapter for an overview of neoclassical explanations of the subprime and financial crises.

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