



11350 Random Hills Road, Suite 800, Fairfax, Virginia 22030 Phone (703) 934-6101 Fax (703) 352-3678

fff@fff.org www.fff.org

Clueless Obama **by Sheldon Richman**

If President Obama doesn't understand why the economy tanked, he surely won't know what recovery requires. And if he doesn't know that, he's surely part of the problem, not the solution. In his speech on the economy at Georgetown University this week, Obama again showed that he hasn't a clue what caused the economic calamity. He spent a few paragraphs of his speech "explaining" to the students what happened — but he got it wrong. Had this been a class, he should have gotten an F.

According to Obama, instead of having to save to buy a house, "many Americans found they could take out loans that by traditional standards their incomes just could not support." No explanation of why they were able to "find" this. He continues: "Others were tricked into signing these subprime loans by lenders who were trying to make a quick profit. And the reason these loans were so readily available was that Wall Street saw big profits to be made. Investment banks would buy and package together these questionable mortgages into securities, arguing that by pooling the mortgages, the risks had been reduced. And credit agencies that are supposed to help investors determine the soundness of various investments stamped the securities with their safest rating when they should have been labeled 'Buyer Beware.'"

Obama goes on to explain that "No one really knew what the actual value of these securities [was], but since the housing market was booming and prices were rising, banks and investors kept buying and selling them, always passing off the risk to someone else for a greater profit without having to take any of the responsibility."

Why people bought assets of uncertain value and thought housing prices would never fall, Obama doesn't say.

"Banks took on more debt than they could handle. The government-chartered companies Fannie Mae and Freddie Mac, whose traditional mandate was to help support traditional mortgages, decided to get in on the action by buying and holding billions of dollars of these securities. AIG, the biggest insurer in the world, decided to make profits by selling billions of dollars of complicated financial instruments that supposedly insured these securities. Everybody

was making record profits — except the wealth created was real only on paper. And as the bubble grew, there was almost no accountability or oversight from anyone in Washington. Then the housing bubble burst.”

What’s missing from the story? The government’s indispensable role in initiating the bubble. Americans were able to buy homes without savings, down payments, or even incomes because government agencies encouraged and even mandated lower lending standards for people who could not qualify for traditional mortgages. The lower standards also enabled creditworthy people to borrow more than their incomes would have previously allowed. This was all a deliberate government policy, which stimulated demand and inflated the bubble.

The shaky mortgages were indeed packaged as securities, but again Obama omits the government’s key role. Many mortgages were guaranteed by government agencies, giving investors safety they couldn’t find elsewhere. The AAA ratings for these dubious instruments were issued by the three members of a government-sponsored rating cartel, which issuers of securities by law had to use. AIG’s credit default swaps insuring those securities arose in this government-constructed environment, adding to the illusion of safety.

The closest Obama gets to mentioning a government role is his reference to “government-chartered companies Fannie Mae and Freddie Mac.” But these are more than government chartered. They are privileged corporations with implicit government backing. Members of Congress and officials at the Department of Housing and Urban Development pressured them into buying more and more dubious subprime mortgages, which they sold as bundles of safe securities or held for themselves.

Obama also left out the Federal Reserve, which contributed to the bubble perhaps by holding down short-term interest rates and certainly by promising liquidity to overextended banks.

The government did not merely fail to provide oversight. It actively created this fragile situation, which had to collapse. Remove government from the picture, and there is no bubble or financial collapse.

Obama promised that “we will hold accountable those responsible.” If he means it, he will start with the government agencies that made this mess.

*Sheldon Richman is senior fellow at The Future of Freedom Foundation, author of **Tethered Citizens: Time to Repeal the Welfare State**, and editor of [The Freeman](#) magazine.*

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