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“Property Bubbles, Housing Provision and Welfare State Reorganization in the United States and Europe,”  
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**Abstract:**

Why did the current financial crisis emerge from the U.S. housing finance system, and how did that relate to political efforts at welfare state reorganization in the 1990s and 2000s? This chapter assesses these dynamics in the context of the globalization of markets for mortgage-based assets. U.S. and European efforts at welfare state reorganization typically involved both institutional and attitudinal changes. Political actors and states tried to introduce market or market like mechanisms and attitudes into programs and institutions that previously had been decommodified or operated on a citizen right basis. In housing, generally, this involved a shift from public rental support and other forms of public housing to support broader homeownership, as well as the introduction of mortgage securitization. Attitudinally, it involved transforming citizen-recipients into more active subjects who created their own welfare state and particularly pensions via individual asset-holding. This encouraged people to treat housing as a speculative asset or a discretionary rather than forced savings vehicle. Both the institutional and attitudinal changes dovetailed with bubble era efforts to ‘reform’ the basic old age pension by individualizing and then perhaps privatizing it.

The U.S. and Europe differed in systematic ways in the degree of mortgage securitization, and, to a lesser extent, attitudinal changes, which also explains the differences in their experience of the current financial crisis. In the U.S., the steady expansion of Fannie Mae and Freddie Mac substituted securitization for a European-style housing policy based on state or cooperative ownership. Similarly, the 1990s Community Reinvestment Act and the 2000s subprime mortgage bubble represented risky but politically driven efforts to capture low income constituencies respectively for the Democratic and Republican parties, rather than a full fledged national housing policy. But securitization and the politically strategic use of housing policy were also found in some European countries, because access to housing – already a ‘wobbly pillar’ of the welfare state – was a source of rising class and inter-generational inequality in both liberal and social democratic welfare states. That said, most European financial problems came from exposure to securitized US mortgages, not local ones. The current crisis reverses welfare state reform trends everywhere, creating permanent barriers to privatization of housing and pensions. The renationalization of Fannie Mae and Freddie Mac provides an opening for the Obama administration to pursue a more European style housing policy, but this is unlikely to take the form of more publicly owned housing. Similarly, while many European states will now slow their already tepid efforts to introduce Danish or German style securitization, they are unlikely to expand public housing. In many ways the crisis seems likely to act as a ‘reset’ button, restoring the housing policy status quo of the 1970s, before welfare state reform started in earnest.

## 14: The politics of housing provision and property bubbles in the United States and Europe

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The current global financial crisis seems to belie many predictions by conservative (and some left) critics that the welfare state would bring capitalism to its knees. The current crisis originated at the intersection of high finance and the housing finance system, and moreover in the United States, which has the most limited formal welfare state of the rich OECD countries and one of the lowest rates of publicly owned housing. Housing has always been considered the “wobbly pillar” of the welfare state, reflecting a low degree of decommodification and a high degree of emotional attachment by owner-occupants (Torgersen, 1987; see also Lowe, 2004 and Langley, 2008). This chapter explains why the financial crisis emerged from housing finance systems, particularly US housing finance, and how the crisis is connected to political struggles around the welfare state. It does so in four steps. Analytically, the first three sections focus on the decommodifying, stratifying and partisan consequences of different housing finance systems.

First, the chapter surveys and expands on the literature on housing and the welfare state to show how pensions and housing finance systems interact to decommodify access to housing in greater or lesser degrees. Second, it describes the structure and deregulation of housing finance in the United States, paying particular attention to the rapid increase in the securitization of mortgage debt in the late 1990s, and contrasting this with financing systems in Europe. Greater securitization in general permitted – indeed encouraged – greater stratification. Third, it looks at the specific politics that drove up the rate of homeownership and thus also housing debt in the United States. Both US political parties consciously expanded access to housing finance to bid for voter loyalty. Because new homeowners disproportionately had low and volatile incomes, the combination of rising homeownership and more securitization created the conditions for widespread defaults that damaged both the financial system and living conditions for the two bottom quintiles by income. Finally, the conclusion argues that the financial crisis will act like a ‘reset button’ for housing finance in the most liberalized rich OECD economies. A renewed government presence in the supply of housing finance will return housing to its original condition of wobbly pillar by re-establishing standardized mortgages and dissuading people from treating their houses as a speculative asset, ATM (i.e. cashpoint machine), or a mechanism for substantial intergenerational wealth transfer. Nevertheless, this will reinforce stratification in liberal economies by excluding those whose credit rating does not qualify them for a standard mortgage.

### 1: Housing and the welfare state

#### 1a: Existing Literature

Jim Kemeny (1980) and Frank Castles (1998) generated the classic arguments about the inverse relationship between owner-occupied housing and the development of the welfare state. Gösta Esping-Andersen (1985; see also Allen, 2006 who tries to update Esping-Andersen) U. Torgersen (1987) and David Malpass (2008) present narrower arguments about the partisan use of housing policy. More recently Schwartz and Seabrooke (2009) have tried to update these arguments and integrate the politics of housing financial systems with comparative political economy. In general, the central issue in all these arguments is the degree to which decommodified access to housing helped support decommodification more generally in other welfare state arenas. Kemeny (1980) argues that the greater the degree of private ownership, the weaker the entire welfare state will be. Castles’ (1998) claim is narrower: higher levels of private homeownership produce weaker and smaller public pensions, particularly second tier pensions.

Kemeny (1980) argued for a trade-off between owner-occupation of residential property and the quantity and quality of welfare state benefits. For him, the front loading of housing costs for owner-occupiers inclined them against higher taxes for social services and transfers. While the total life-cycle cost of owner-occupied or rented housing was the same at any given level of income for a society or a specific individual there was considerable temporal variation. Would-be purchasers of owner-occupied housing have

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<sup>1</sup> The author would like to thank Gerard Alexander, Joseph Cordes, Lindsay Flynn, Christian Toft, ETC for very useful comment and criticism. All errors remain mine unless I can put them behind the wallboards during my next renovation.

to save for a down payment varying from 10 to 50 percent of the purchase price and then face a front-loaded schedule of payments as they amortize a mortgage over the next 15 to 30 years.<sup>2</sup> Buying a house thus compresses the bulk of the life-cycle cost of housing into a household's early years. This compression can be seen in high home-owning America, Britain and Norway, where the median debt level for the 35 to 44 year old cohort ranges from nearly \$50,000 to nearly \$70,000 (Table x.1 provides some descriptive statistics on housing systems). By contrast, renters essentially make level payments each year. Childbearing typically occurs at roughly the same time that incomes are rising; symmetrically, as children depart at the end of the life-cycle, both income and rental costs could fall. Moreover, renters often benefit from regulations that slow rent increases and secure something amounting to life-time tenure, as in the Netherlands or Germany. Kemeny thus argued that the level of home ownership was not a natural outcome of rising or high per capita income levels, but instead reflected political choices by voters and parties. High-income economies like Denmark and Germany could exhibit low levels of home ownership if politics and policy favored social spending, including social housing, over private homeownership (Kemeny, 2005:60).

Table x.1: Descriptive statistics on housing finance for select OECD economies, 2000s (pre-crisis)

	Home-ownership rate 2006	Typical Loan To Value Ratio	Typical Loan to Income Ratio	Average Loan Term in Years	Mortgage debt as % of GDP 2006	Default Rate (%)*	Median debt of 35-44 year olds in 2002 USD
Netherlands	54.0	90	3.4	30	102.7	0.6	
Denmark	54.0	80	3.2	30	88.6	1.3	
Spain	86.3	70	2.7	20	58.6	6.0	
UK	70.0	69	2.2	25	83.1	1.0	65561
France	56.5	67	1.4	17	32.2	2.8	
Germany	43.2	67	n/d	23	51.3	n/d	
Italy	80.0	55	0.9	15	18.7	5.2	
United States	69.0	90	3.6	30	78.0	2.0	49769

Source: European Mortgage Foundation 2001; Neuteboom 2003; 2004; Federal Housing Finance Agency at <http://www.fhfa.gov>; last column, OECD, *Growing Unequal: Income Distribution and Poverty in OECD Countries*, Paris: OECD, 2008, p. 260. n/d = no data; Loan to value = what percentage of the house's value can you borrow?; Loan to income = how big can the loan be relative to household income? \* = pre-crisis default rate

Frank Castles (1998) provided a more focused causal argument with a more precise micro-foundation. Castles argued for a specific trade-off between individual homeownership and robust pension spending (see also Conley and Gifford, 2006). Housing generally constitutes not only the greatest single item in most retirees' budgets, but also, with food, one of the least substitutable or dispensable. The imputed income from freehold homeownership substituted for public pension income. Causally, settler societies with high levels of homeownership prior to the emergence of public pension systems were least likely to develop robust public pensions, because freehold ownership of housing substantially reduced the income requirements of the home-owning elderly. Echoing Kemeny, Castles also noted that better off parts of the elderly population were more likely to own houses and thus were less favorably disposed towards higher taxes to provide cash income to elderly renters. In addition, while both renters and owners bear the cost of property taxes, these taxes are most visible to owners, and thus draw the most resistance (Martin, 2008). Homeownership splits the natural elderly constituency for expanded social spending.

<sup>2</sup> The United States, where "zero down payment" mortgages are available, and Japan, with its 50 year mortgages, are obvious exceptions. Nevertheless, even in the United States a minimum 10% down payment is required to get the best (lowest) interest rate.

### 1b: The United States as an example

While Castles and Kemeny disagree on details, they agree that via down-payments and mortgage payments, widespread homeownership crowds out taxes early in a voter's life-cycle. Housing, housing finance, and pensions in the United States exhibit the classic Castles trade-off while also affirming some of Kemeny's arguments. Widespread homeownership, early acquisition of homes, and high levels of mortgage debt are paired with a mildly redistributive basic public pension (demotically, "Social Security"; officially, the Old Age, Survivors, and Disability Insurance program) and a highly stratifying second tier pension. In this system, homeownership is not just a supplement to pensions but rather a crucial leg of a three-legged pension stool. The first leg of the pension stool is of course, Social Security, which functions as a basic, minimal citizen's pension. The second leg is tax privileged, but private, second tier pensions, the vast majority of which are occupational defined benefit or defined contribution pensions. Defined contribution pensions include the so-called '401k' and '503b' tax deferred savings vehicles sponsored by firms, as well as individual retirement accounts (IRAs). About half the US population does not have effective access to this second leg. Only 21 percent of workers are covered by traditional employer based defined benefit plans – which anyway are vulnerable to corporate bankruptcy. About 55 percent of workers – who partly overlap the first group - have access to a 401k account, but many have incomes too low to fund them adequately. By contrast, roughly 80% of American households aged over 65 (and 90% of elderly white households) own their home, making homeownership more widespread than access to a robust second tier pension (Englehart, 2007:52; Harvard JCHS, 2009:14).

American pensioners' outright home-ownership matters because their post-market incomes from secondary pensions are so weak. Nearly three-fifths of American households over age 65 had cash incomes under \$35,000 in 2008 (versus a US-wide median of \$50,300 and an over 65 median of \$29,000) (US Census). Given that almost all households with two former workers who together had earned the median income could expect about \$20,000 in Social Security payments, while two former workers at the 75<sup>th</sup> percentile (about \$95,000 former household income) could expect \$30,500 in Social Security payments, the bulk of retired households with incomes under \$35,000 were probably living solely on Social Security. The remaining 40 percent of households have some secondary pension income. But three-fifths of those households have incomes under \$70,000 (median income circa \$50,000), implying that the avoided cost of housing looms large.

The federal government supported homeownership with a mix of programs that affect the supply and price of credit, the production of housing, and buyers' ability to service mortgage debt. These programs were highly stratifying through the underwriting criteria they established for mortgages. Those criteria historically favored and shaped a largely white middle and upper class population. Roughly speaking, those criteria helped divide American pensioners into three groups: those with Social Security but no home; those with Social Security, a home and a derisory second tier pension; and those with all three legs of the pension stool. Non-home-owning households are less likely to have access to a robust second tier pension and more likely to face excessive housing costs. Among American pensioner households in 2008, 38% of those relying solely on Social Security for their income spent in excess of 50% of their income for housing, while only 12% among those with second tier pension income faced this stress (Harvard JCHS, 2009:3). In these circumstances pensioners may present a unified front against cutbacks to the basic pension, but are divided over any tax financed expansion of public housing, which might devalue their own property holdings, or a new public second tier pension, which might involve increased taxation of private pension income.

There is thus reason to see a commodified housing sector as a permanent roadblock to a universal welfare state (Lowe 2004). Yet, the correlation is not one for one, suggesting that the Castles/Kemeny analysis has some problems that arise from its focus on welfare state formation rather than the dynamics of societies with growing homeownership rates and greater household exposure to housing market dynamics (Malpass, 2008:xx). First, a commodified housing sector may create demands for state intervention in both traditional and non-traditional welfare issue areas. Buying a house commits a household to large monthly payments with large transaction costs if one must exit the purchase. Failure to make payments can lead to foreclosure, loss of one's down-payment (purchase money), and a damaged credit rating. Ideally, one would want to match a long term stream of payments to a long term stream of income, particularly if those

payments were high in proportion to one's income. Most countries with high levels of mortgage debt in relation to incomes have several public mechanisms for reducing those risks. These include overt welfare state programs such as unemployment insurance with high replacement rates (which favor higher income earners who are likely to own houses); employment protections to reduce the risk of being fired; and relatively low transaction costs (which make it easier to sell a house in distress). Even the United States has its usual 'hidden welfare state' (Howard, 1999) variations on this theme: the widespread availability of fixed rate mortgages with relatively low down-payments means that the average home-buying household faces no interest rate risk and has little cash tied up in the house if unemployment occurs in the early years of home-ownership. These mortgages exist because the state sponsored mortgage giants, Fannie Mae (FNMA – the Federal National Mortgage Association) and Freddie Mac (FHLMC – the Federal Home Loan Mortgage Corporation) shifted the mortgage market away from the 'high down-payment, fast amortization, variable interest rate' mortgage model found in most European economies.

Second, societies with high levels of homeownership and very liberal mortgage markets are just as likely to have large socially rented sectors as those with controlled mortgage finance. Thus in Denmark, post-Thatcher Britain and the Netherlands, socially-rented housing accounted for over 20 percent of the entire housing stock and in excess of half of the rental stock in the early 2000s, even though these countries have relatively liquid, deregulated and market based housing finance systems. By contrast, in high owner-occupier Italy, Spain and Ireland, all of which have relatively illiquid and controlled housing finance systems, the social rental sector accounts for less than 10 percent of all dwellings and less than half of an already relatively smaller rental stock (EU, 2003). In addition, default rates are high in Italy and Spain, suggesting significant vulnerability to income shocks. Simply looking at the level of owner-occupancy does not tell us how homeowners are exposed to the market. What matters is their level of debt and the associated monthly payments on that debt. US homeowners in general spend less of their household income for housing than most Europeans.

### 1c: Updating the literature

Schwartz and Seabrooke (2009) address these issues by arguing that the scale of mortgage debt and the rate of homeownership interact to produce four different types of housing markets and thus four different flavors of Castles/Kemeny trade-off. They label these as social-corporatist, liberal market, catholic-familial, and statist-developmental housing markets. Each type has a distinct set of institutional complementarities linking combinations of homeowner political behavior, state intervention in the housing financial system and the welfare state (particularly pensions). These then produce divergent levels of debt, ownership, and social provision. Figure x.1 scatter plots economies based on their deviation from the average OECD level of home-ownership and mortgage debt in relation to GDP. Figure x.2 presents data on average ownership rates, debt and debt finance costs for each type as well as housing debt and costs in relation to disposable personal income, which is a better measure of the effects on individual households.

Figure x.1 Relative deviation from average OECD levels of mortgage debt to GDP and owner-occupation prevailing 1992 to 2002 (percentage points)

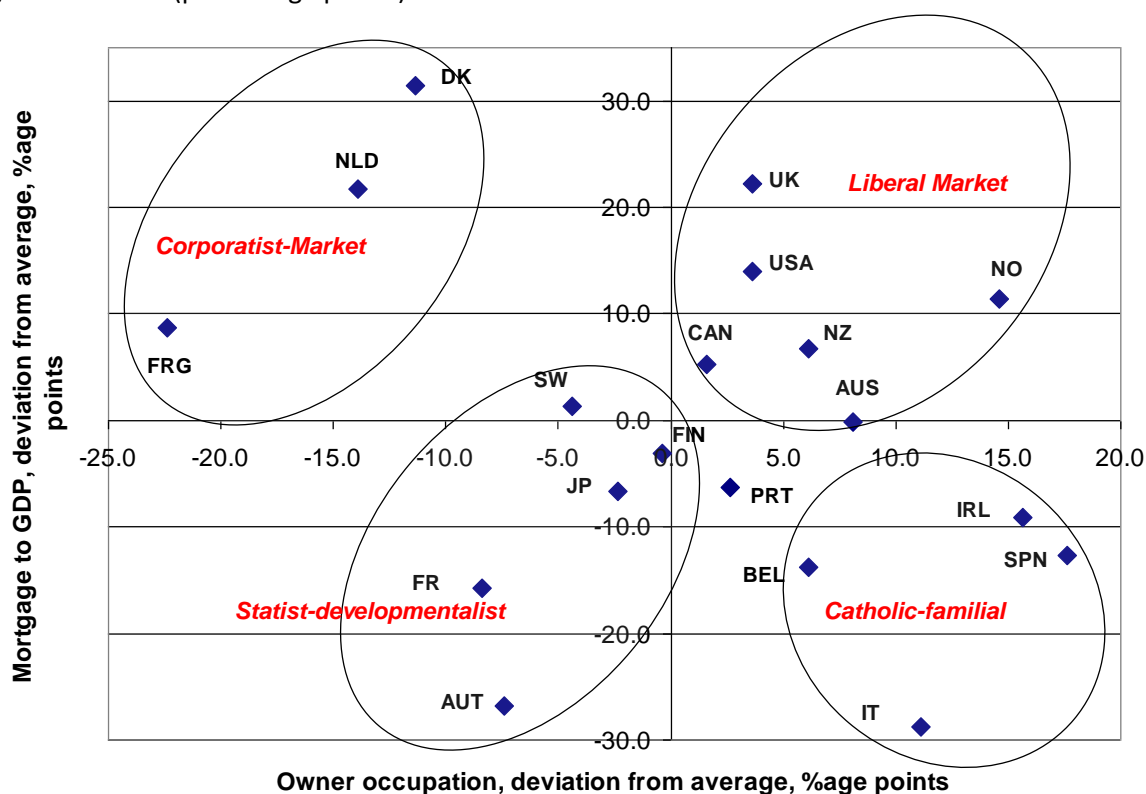


Figure x.2 Average levels of home-ownership, social rental market, mortgage debt in relation to GDP, and mortgage interest costs in relation to disposable personal income (DPI) in four types of housing markets for 19 OECD countries

		Owner-occupation Rate (average of 1992 and 2002)	
		Low	High
Mortgage debt as a % of GDP (average of 1992 and 2002)	High	<b>Corporatist Market</b> Mortgage debt::GDP: 58.3 % Mortgage Debt::DPI: 86.4 %* Interest Costs::DPI: 4.3 %*  Owner-occupation: 47.0 % Social rental: 20.7 %	<b>Liberal Market</b> Mortgage debt::GDP: 48.5 % Mortgage Debt::DPI: 72.0 %* Interest Costs::DPI: 4.7 %*  Owner-occupation: 70.1 % Social rental: 9.4 %
	Low	<b>Statist-developmental</b> Mortgage::GDP: 28.2 % Mortgage Debt::DPI: 48.0 %* Interest Costs::DPI: 2.0 %*  Owner-occupation: 58.3 % Social rental: 16.8 %	<b>Catholic-Familial</b> Mortgage::GDP %: 21.6 Mortgage Debt::DPI: 26.1 %* Interest Costs::DPI: 1.1 %*  Owner-occupation: 75.5 % Social rental: 5.5 %

\* Weighted average using 2003 purchasing power parity share of OECD GDP; all other averages are unweighted.

Source: Compiled from OECD 2005a: 131.

The typical liberal housing market features an elaborate set of public policies often outside the formal welfare state that support widespread home-ownership, rather than an absence of state intervention *per se*. They are thus 'liberal' only by contrast to the statist group, which directs finance away from individual housing and towards manufacturing. The liberal states typically subsidize(d) owner occupation through mortgage interest tax deductions, while dedicated financial institutions like Fannie Mae and Freddie Mac lower mortgage interest rates. Subsidies and easy access to housing finance combine with abundant land to produce surprisingly low house purchase costs in relation to income. While the other three types have lower interest costs (Figure x.2), their total housing costs are typically higher.

In the liberal systems, commodified access to housing reinforces income and wealth stratification. Households with robust private pensions also typically have robust savings and more expensive houses and, often, more houses period. Secondly, intergenerational wealth transfers reinforce wealth inequality, as deceased parents' houses are transformed into liquid assets. These dynamics can be seen strongly in New Zealand, where a near total liberalization of residential property finance has led to a significant *decline* in home ownership as upper class and foreign investors squeeze out the lower-middle and working classes (Broome, 2009). Similar dynamics are at work in Australia, where tax regulations favor private ownership of rental property (Seabrooke and Mortensen, 2009), and Norway, where deregulation of cooperative housing allowed owners to capture capital gains through private sales (Tranøy, 2009). As Seabrooke puts it, in these countries, up until the 2007 property crash, the old appeared to be eating their young. The old captured both rising housing equity and share values through their private pensions, while the young faced low wages, weak pension schemes and a lifetime of renting. The subsequent collapses in property prices may re-establish the stability of the traditional mix of broad home-ownership plus weak pensions. Even so, the parallel with insider-outsider stratification in the Familial markets is striking.

The high taxation, corporatist countries of Denmark, Netherlands, and Germany do not have widespread property ownership. Consistent with the Castles/Kemeny models only about half of households own property, while the state provides generous social support in old age in addition to a wide range of social support. This includes a wide range of socially owned housing; 35 percent of Dutch housing units are socially or cooperatively owned. Even in Germany, where only 6 percent of the housing stock is socially owned, intrusive regulations on tenure, rent increases and quality secure renters of private dwellings from rental shock and displacement. Rental costs are homogenized via the principle of *vergleichsmiete*, which sets rents for comparable rental units regardless of who owns them.

Mortgage debt levels in relation to income or GDP in Denmark and the Netherlands are much higher than in the United States. Denmark, for example, has a residential property based covered bond (pantbrev) market that relative to GDP dwarfs that in the United States. High tax levels also fund a generous and more egalitarian welfare state than the one in the US or most liberal housing economies. Why hasn't this debt sparked political conflicts over taxes and interest rates? High levels of taxation are accompanied by large tax breaks for property ownership, and the high level of taxation makes these tax breaks attractive. The highest individual marginal tax rate is 63 percent in Denmark, versus a more typical 45 percent rate. These rates make housing attractive as an investment vehicle for those with high and stable incomes (Mortensen and Seabrooke, 2009). Against this, well funded health care and education systems make upward mobility much easier for the children of lower income groups. Danes also paid more than double what the Swedes paid in interest payments as a percentage of disposable income in 2003 (8.3 percent in Denmark compared to 3.3 percent in Sweden (OECD 2005a: 203)). In Germany, mortgage finance is more restricted. Pfandbrief (covered mortgage bonds) can only be issued at a 60 percent loan-to-value ratio, and combined with an average price to income ratio of 6.2 this means that few families can save enough for a down payment. Here too, however, taxes and tax subsidies favor investment into rental properties, alleviating the shortages usually subsequent to rent control. In particular, rental properties are free of capital gains taxes, though admittedly German property prices have been soft for a decade. The state thus internalizes two offsetting transfers whose net effect is a concentration of property ownership into private, non-corporate hands.

The catholic-familialist housing systems of Italy, Belgium and Iberia, also strain the classic Castles/Kemeny argument. These systems combine generous state spending for some pensioners with high rates of homeownership. Here newly formed households face both taxation to support the old, plus an

illiquid housing market that until recently required large down-payments and provided only short-term mortgages (see Aalbers, 2009b on Italy; Allen, 2006). As Castles and Ferrara (1996) have forcefully argued, Southern European welfare states can defy the predicted housing versus pension trade-off only by constraining public spending on other welfare programs or by running up massive deficits. Instead, the trade-off is between housing and non-pension spending. In these countries intergenerational transfers favor pensioners at the expense of the young, or they exclude non-core workers from public pension schemes. The result is delayed household formation (which raises the homeownership rate but lowers the fertility rate) as the young face both high taxes and lack access to the easy housing typical of the liberal system. Not only is homeownership above the OECD average in all the catholic-familial systems, but the proportion of families (households with children present) to total households is also above average (Allen, 2006:224-6). These systems also lacked securitization until recently. Although Italy and Spain relaxed mortgage origination rules and introduced securitization in the 2000s, the 2008 financial crisis will probably make lenders (and securitizers) once again cautious about extending mortgage credit. In 2007, residential MBS issues amounted to €55 billion and €22 billion in Spain and Italy, as compared to €35 billion in the much smaller Netherlands and €139 billion in Britain (EMF, 2007:77).

Consequently the family and the black economy play a symbiotic role in housing and welfare provision in catholic-familialist housing systems. Families use housing as a tax-opaque vehicle for intergenerational wealth transfers that eventually, unevenly and erratically return government spending to the overtaxed young or non-core workers. Families pool both monetary and physical resources to help younger generations enter the housing market, albeit after very long sojourns in the parental house. This self-help tradition contributes to lower tax receipts. A substantial share of the housing supply in Italy is not properly registered, magnifying the effects of the black economy and migrant remittances (Castles and Ferrara, 1996: 178, 182-83). Much housing is built illegally, without planning permission, and with black market labor. Housing finance thus reinforces the stratifying effects of the formal welfare system, which divides labor market insiders from outsiders.

The statist-developmental systems – France, Austria, Japan, Finland, and, at a distance, Sweden – also exhibit a specific trade-off, although Uzuhashi (2003) argues that Japan shares some features similar to the catholic-familialist group. Here, the rate of homeownership is low, and mortgage debt and mortgage interest payments are relatively low as a share of personal income. The state provides a robust basic public pension and compels workers to join publicly organized secondary schemes. Consequently, there is no flow of private pension money to support an expansion of housing and housing debt through recycling into MBS, as in the liberal housing economies. Instead, the statist systems have relatively high levels of state owned housing – particularly Sweden – which allows the state considerable control over the volume of capital allocated to housing. The state limits capital flows to housing in order to channel capital preferentially to the manufacturing sector. All of these states have above OECD-average levels of manufacturing employment, and what are essentially tax-financed PAYGO pension systems.

Intergenerational transfers are thus much more straightforward in the statist systems, with the state shifting money from young to old via taxation, rather than the more opaque and unequal transfer via the housing market in liberal market and catholic-familialist systems. This permits much greater amelioration of poverty, although the Japanese system is somewhat regressive. Large scale provision of public housing in all but Japan reduces financial pressures on lower income retirees, while increasing tax pressure on the young. Like the liberal housing economies, the statist-developmental ones exhibit a clear pensions-home ownership tradeoff, but unlike them the state is heavily involved in constructing social or semi-social housing to buffer the old and poor against income shocks. This largely takes the form of rental units, as Pollard (2009) shows for France, and as demonstrated in Sweden's *miljonprogrammet* (which built over a million apartments and houses in one decade). In Japan, companies with financial backing from the state built a considerable portion of the housing stock in the new industrial towns that emerged after World War II. Japanese public pensions are smaller than might be expected because elderly Japanese often cohabit with their adult children, passing along ownership of the house as the children's reward for providing care. This is one reason Uzuhashi (2003) see similarities to the catholic-familial model.

Recent data from the Luxembourg Wealth Study might seem to contradict the typology and argument above. These data show that non-financial wealth – the bulk of which surely must be housing – constitutes a somewhat larger share of household portfolios in countries like Italy, Germany, and Finland, than they do in countries like the United States, Canada and Sweden (OECD, 2008: 259). Surely this implies that homes much loom larger in people’s calculations in the first set rather than the second set? But this interpretation of the data ignores the salience of public second tier pensions in the first set of countries. While public pensions are not counted as part of household wealth, they surely loom large in people’s mental calculation of how much wealth they need to accrue for retirement. These calculations, as well as the higher taxes that support public second tier pensions, reduce private saving via financial assets. In effect, the state has captured the ‘financial asset’ part of the typical household’s portfolio in those countries. As a result, homes represent a relatively smaller share of household wealth in the United States not because households decline to use them as a savings vehicle, but rather because they must save so much in other forms to compensate for the missing public second tier pension. Thus Americans on average hold 50 percent to 100 percent more of their savings in financial instruments as compared to these other societies. Looking at the median person makes this even clearer: the median person in the United States and Canada holds about 60 to 80 percent more by value in non-financial assets than the median German or Swede (OECD, 2008: 265, 277). Unfortunately, there is not enough data currently available to do a systematic analysis.

## **2: Financialization, securitization and welfare reform in relation to housing**

### 2a: Securitization

Like all typologies based on institutional complementarities, the one above is overly static. While it highlights and clarifies the different ways in which access to housing is commodified, it obscures how continual efforts to individuate risk and reduce citizen based welfare have moved housing to the forefront of individual strategies for attaining economic security. Put simply, rolling back or transforming the transfer and service parts of the welfare state raised the pressure on individuals to use their houses to manage their life risks. The more successfully welfare state opponents were in shifting risk off the fisc and onto individuals, the more those individuals came to rely on houses as a source of current and future consumption, emergency cash, and disguised retirement savings. This individuation of risk and the financialization of housing meet in the process of mortgage securitization.<sup>3</sup> Conversely, the MBS created by securitization necessarily have as their counterpart and counterparty large private pension and insurance funds seeking stable long term returns to fund their on-going obligations. These firms make the market that buys MBS on a routine basis. Thus cash flows from people servicing mortgages to those enjoying pensions, which on average means a transfer across generations from young to old. This process has been fairly stable for the past 50 years in countries that have liberal housing markets and private pensions, and particularly in the United States. What changed was the volume of transactions and the distribution of risk.

The differing uses and politics of mortgage securitization in the United States demonstrate the shift from risk socialization to risk individuation. Under a fordist politics, mortgage securitization either did not occur or occurred in relatively limited and publicly controlled amounts, and supported a standardization of housing and housing opportunities for the broad (white) middle class. The state provided direct and indirect support for standardized housing through the Federal Housing Administration, which, with the Veterans Administration funded as much as half of all mortgages in the 1940s and 1950s (Gramlich, 2007: 14), through Fannie Mae and then Freddie Mac, and through generous tax deductions for owner-occupier mortgage interest (Howard 2006). Prior to deregulation, pension funds had sought long term returns by directly building and operating large real estate complexes. Thus in the 1940s Metropolitan Life Insurance company built over 20,000 apartments in the Peter Cooper Town-Stuyvesant Village and Riverton complexes in New

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<sup>3</sup> Securitization bundles large numbers of mortgages together – usually 500 to 1000 – and sells the rights to income from this bundle to the capital market. In effect, in its simplest form, it transforms individual mortgages into a kind of corporate bond. Banks originate mortgages, and then sell them to investment banks or public housing banks (like Fannie Mae) that create and market these new securities. Then banks have cash in hand to originate new mortgages again. Banks have an incentive to securitize mortgages because it removes interest rate risk from their books and allows them to make more transactions, and thus more fee income from transactions.

York City. Fannie Mae's purchase and eventual securitization of mortgages permitted pension funds and insurance companies to diversify their risks and purchase a pure financial asset, leaving real estate management to owners and real estate firms. Until the 1970s, Fannie Mae and Freddie Mac bought mortgages and held them to maturity, and in turn provided a safe investment for pension funds by selling their own bonds to those funds. These quasi-public firms had an implicit government guarantee that was validated in the summer of 2008. This guarantee permitted the 'Frannie' twins to float trillions of dollars in bonds and eventually mortgage backed securities (MBS) on a very thin capital base. In turn, this made possible the very buyer/debtor friendly dominance of callable, fixed interest rate, no-recourse loans that dominate the US market, in contrast to nearly every other market (see Table 1.1). The Frannies' MBSs constituted a fairly consistent third of the US private securities market from the mid 1990s onward, energizing a transactions oriented financial sector. In turn, this helped buoy housing prices in the United States, shifting wealth towards housing market insiders and validating personal strategies of wealth accumulation based on housing.

On the borrower's side, Fannie Mae's (and Freddie Mac's) policy of only purchasing loans that conformed to their underwriting standards targeted and created a homogeneous suburban white middle class. Conforming (i.e. 'prime') loans required borrowers to make a 10 percent down payment (i.e. have a 90 percent loan to value ratio), have a credit rating that put them into the top 70 percent of the population, and expend no more than 28 percent of their gross income on direct housing expenses (principal, interest, property taxes and insurance). In addition the loan amount was capped in most markets at 125 percent of the national median home price. These criteria assured very low default rates on these mortgages. Default losses in MBS pools built on conforming mortgages were shared equally by all purchasers of the pool. The Frannies' direct bond issuance and securitization thus homogenized debtors and creditors, while socializing risks.

## 2b: Financialization

As fordism gave way to neo-liberalism and financial deregulation, the majority of mortgages were already being securitized. From 1988 to 2006, new issues of MBS rose from \$165 billion to \$2047 billion. But the originators of and the vehicles for securitization changed as financial deregulation permitted investment banks and other financial firms to enter the Frannies' territory. Private securitizers took ever increasing shares of the market up until 2006, rising from 9.1 percent in 1988 to 55.7 percent. They sold securities that individuated risks rather than socializing them. Private-label MBSs did not offer investors a pro-rata share of payments from a given pool of mortgages; instead, the underlying pool of mortgages was sliced up into tranches of Collateralized Debt Obligations (CDOs) in order to offer investors differing degrees of risk and reward, as well as maturities at variance from the underlying mortgages. CDOs concentrated risk into the lower rated tranches of the CDO. Here, losses could wipe out an investor holding those riskier tranches – as happened in 2007-08. Why might losses occur? Generally, defaults occur when home buyers suffer a sharp loss in income or a sharp increase in payments or, as happened in 2006-07, both. On the borrower's side, loose underwriting criteria meant that would be home owners could easily take on much more debt than they could sustain even in a benign economic environment, let alone a downturn.

Why did borrowers willingly take on that debt? In an environment in which private second tier pensions were shifting from a defined benefit to defined contribution basis, and in which fewer firms even offered any pension at all, housing's role as the third pension leg rose in importance. Housing finance systems characterized by high levels of home ownership can potentially gift huge capital gains and enhanced consumption to incumbent homeowners if they are able to treat their house like an asset. Securitization enables this if to be realized, by making housing finance markets more liquid, expanding the potential for the cash out of home equity in pursuit of expanded consumption, and encouraging more lending against property. Securitization thus permits – but does not force – households to leverage their housing investment by having a small down payment and a large debt. When housing prices are rising, households that make this choice can accumulate assets much, much faster than unleveraged households. At the same time – as we now see – borrowers are also exposed to global interest rate shocks, abrupt de-leveraging, and the loss of wealth in a downturn. Even in relatively decommodified housing markets, like Norway, the potential for very

large capital gains can induce owners of social and quasi-social (e.g. coops) housing to seek the commodification of that housing in order to cash out those gains (Tranøy, 2009). Thatcher hoped for a similar dynamic when she made it possible for tenants to purchase their Council (i.e. public) homes in Britain; by contrast Social democratic parties sought to prevent this dynamic through their housing policies in the 1960s and 1970s (Esping-Andersen 1985).

The conventional wisdom reinforced would-be homebuyers' rush into the market. Unlike in Britain, where a quasi-official discourse encouraged people to become asset owners in order to manage their own retirement (Watson, 2009; Langley, 2008), in America a bevy of financial media and self-interested industry groups promoted homeownership at any price. For example, as late 2006 David Lereah, the chief economist for the National Realtors Association, and author of *Why the Real Estate Boom Will Not Bust and How You Can Profit From It*, was saying that anytime was a good time to buy homes. Similarly, financial advice columnists in the popular media also touted the long run benefits of homeownership for wealth accumulation. All this took place in an environment marked by major state initiatives to boost homeownership among minorities and the poor, both for partisan political reasons and to reduce reliance on state funded, citizen right forms of welfare or risk reduction.

### **3: Welfare and the partisan politics of housing in the United States**

#### **3a: Partisan competition: The terrain**

Partisan struggles over public policy visions for housing provision in the United States demonstrate the fraught connection between housing and welfare, and how the transformation of the risk-sharing, fordist system for housing finance towards a risk concentrating private market system created the conditions for the 2007-09 financial crisis. Real wages stagnated for the bottom 60-70 percent of the US workforce from 1980 onwards. Meanwhile, firms escaped their pension commitments by trimming payments and payouts, shifting from defined benefit to defined contribution plans, and voiding plans through bankruptcy. Homeownership thus became an increasingly important part of people's retirement security; homeowners typically had 5 to 10 times the net worth of non-homeowners (Gramlich, 2007:80-2). Housing wealth also provided two other welfare services. Americans' ability to borrow against their home equity – the value of the house net of the mortgage – gave them a cushion against unforeseen medical or accident expenses not covered by insurance. Second, if house prices rose, houses could also potentially create cashable wealth for retirees if they 'downsized' their housing. Even in the bottom quartile of US households by income, the median family had \$80,000 of home equity in 2007, almost as much as the next two quartiles (Harvard JCHS, 2009:14). Yet homeownership was unevenly distributed. Among elderly households (65 to 74 years old), in 1980 only 59 percent of black households owned their home, versus 76 percent of white households. By 1990 both groups had moved up to 64 and 82 percent, but the gap persisted (Masnick, 2001:29). Moreover, among younger households the rate of ownership was falling and the gap was expanding, signaling future problems. Whereas 57 and 30 percent of white and black households aged 25 to 34 owned (mortgaged) homes in 1980, by 1990 only 52 and 24 percent did (Masnick, 2001:29).

While US politicians did not promote homeownership with quite the same vigor as British politicians (Watson, 2009), they did embark on partisan policies promoting home ownership, particularly for poor black, latino and white voters. Democrats used the Community Reinvestment Act to try to cement black voters' loyalty and secure latino voters' loyalty through increased access to bank-originated mortgages. Republicans similarly tried to detach some – not all – black and latino voters from the Democratic coalition by tolerating a huge expansion of subprime lending by non-depository institutions. (Unlike a bank, a 'non-depository' financial firm is not covered by federal deposit insurance, and consequently is not required to hold the same level of reserves.) Neither strategy addressed the underlying issue, namely stagnant incomes.

These competing housing policies reflected the state of play in US presidential elections. By the 1990s, the Republicans had succeeded in taking nearly all southern white Protestants and many northern urban Catholics out of the Democratic Party's coalition, leaving the parties evenly balanced. Generally speaking, US elections have been won by the party that captures most of the votes of the one-third of white US families that have incomes over \$100,000, as the Democrats did twice in the 1990s and the Republicans did twice in the 2000s. Yet both parties had ambitions beyond simply taking a majority of that group. The

Democrats – whose hold on this well-to-do slice of America has always been more tenuous than their hold on poorer, darker slices of America – sought a permanent majority by removing the race issue. Reforming social assistance programs while moving more blacks into the middle classes through housing policy would defuse white voters' fears that redistribution inevitably favored blacks.

For their part, Republicans had a firmer grasp on the white electorate, winning 54 and 58 percent of white votes in 2000 and 2004. But Republican strategist Karl Rove sought to create a permanent Republican majority by taking away part of the Democratic party's non-white base. Republicans had captured 44 percent of latino votes in the 2004 election, and swelling immigrant populations in all states and especially the southwest made this bloc even more attractive. If the Republicans could capture an additional 10 or 20 percentage points of this vote, the Democrats faced electoral doom in the southwest. Equally so, shaving 10 percentage points off the Democrats' share of the black vote would endanger the Democrats' majority in crucial states like Florida, Ohio and Michigan. In Rove's analysis, latinos and blacks were cultural conservatives and thus halfway to the Republican party. Economic issues, though, drove them towards the Democrats. Like Thatcher, Rove reasoned that turning some latinos and blacks into homeowners might make them economic conservatives as well. Indeed, the drop in the Democrat's latino vote share from 62 to 53 percent, 2000 versus 2004, indicated that this group was biddable.

Both parties saw housing policy as an important lever to capture biddable voters. The Clinton administration tried to expand minority homeownership and close the ownership gap. While lower relative income among blacks and latinos was a continuing cause for lower ownership rates, so also was outright discrimination. As noted above, housing finance in the fordist period produced and reproduced standardized, predominantly white, suburban households and housing products. Government agencies like the Federal Housing Administration and Fannie Mae, as well as private banks, had 'redlined' black neighborhoods, meaning that they simply refused to make loans to potential black owners regardless of their income or creditworthiness. They also explicitly sought to preserve the character of existing neighborhoods by refusing loans to blacks seeking to move into white neighborhoods. The 1968 Fair Housing Act made these practices illegal, requiring banks to lend on the basis of objective measures like credit scores and documented income. De facto, though, both practices continued up into the 1970s. The Carter administration thus passed the 1977 Community Reinvestment Act (CRA) to force banks to behave, first by applying the same lending criteria to all borrowers and second by recycling depositors' money into depositor neighborhoods. The CRA bound only depository institutions – i.e. those whose deposits were covered by federal deposit insurance. The CRA produced a modest improvement in minority homeownership, which reached 42.3 percent of all black households and 41 percent of latino households by 1994 (Harvard JCHS, 2009:37).

### 3b: Democratic Party initiatives

In 1994, the Clinton Administration publicly committed to raising homeownership rates to 67.5 percent of households by 2000, and amended the CRA in 1995 to force banks to stop limiting lending in 'redlined' communities. These amendments did not force banks to make high risk loans, and the amended CRA did not have specific lending targets. However, statistically speaking residents of poorer neighborhoods were more likely to have insecure incomes, shaky credit histories, and smaller down payments. Banks consequently scrutinized these borrowers carefully, knowing that the resulting loans would have to stay on their books, and thus constitute a credit risk for the bank. Given that the CRA contained no penalties for non-compliance (aside from the normal anti-discrimination issues), why did banks comply with CRA? Regulators could use non-compliance to block the bank mergers that proliferated in the wake of financial deregulation in the 1990s. The CRA thus motivated banks to extend credit to low income households. In addition, the Clinton administration pressed Fannie Mae and Freddie Mac to securitize a wider range of loans – though not 'subprime.' By 2000, homeownership rates among blacks and latinos reached 47.6 and 46.3 percent respectively, versus an average rate of 67.4 percent (Harvard JCHS, 2009:37). The Clinton policy created a tight nexus between banks, the community groups that monitored their CRA compliance, and Democratic party politicians in Congress. It thus tied minority elites more firmly to the Democratic party, by showing that the party could deliver jobs and wealth to minority communities. To an extent this was a cyclic phenomenon: in the 1990s gently falling interest rates, gently rising incomes at the bottom, and a robust employment

market created a virtuous cycle in which successful homeownership and income stability reinforced each other.

Nevertheless, this cycle made it possible to also ‘reform’ the social assistance program for single mothers that Americans call ‘welfare,’ namely Aid to Families with Dependent Children (AFDC). Congress changed this program from an unlimited entitlement into a time limited program with strong incentives to and (it was hoped) strong support for going back to work. Spending on AFDC was derisory - \$24 billion in 1996, versus an average \$18 billion annually in agricultural subsidies 1995 to 2006. But politically AFDC was extremely salient, given the popular misperception that it encouraged unmarried black females to get pregnant and live off the public purse. Correct or not, this perception drove white working class voters away from the Democrats and towards the Republicans. The replacement of AFDC by the less visible Temporary Assistance to Needy Families (TANF) program and the invisible Earned Income Tax Credit (EITC) helped remove this issue from popular discourse. TANF generally required recipients to seek training and employment, while the EITC acted as a negative income tax for those able to secure employment. In the robust economy of the 1990s, the number of TANF recipients fell from 12 million to roughly 6 million by 2000, mirroring the rising numbers of minority homeowners. A shift from social provision of housing to a more market based system also paralleled the shift to a more market oriented (‘activating’) system of social assistance. Municipalities began demolishing (admittedly dysfunctional) public housing estates in the 1990s, replacing this with cash transfers for rentals (“Section 8 housing assistance”) and, it was hoped, more private homeownership.

To what extent did this expansion of credit and homeownership create the conditions for the later crisis? While the 1995 CRA revisions permitted securitization of subprime loans, non-depository institutions – those not covered by depositors insurance – were already securitizing these loans in 1995, and CRA securitizations did not start until 1997. The CRA unquestionably facilitated growth in this market, but largely at the margin. CRA lending accounted for only 6 percent of the total volume of outstanding subprime lending in 2007, and CRA loans did not default at rates above the entire pool of subprime loans, indicating that they were not excessively risky (Duke, 2009). Instead, the problems with subprime clearly emerged from the Republican party’s deregulation of depository institutions and non-regulation of non-depository financial firms after 2000.

### 3c: Republican Party initiatives

Like the Democrats, the Republicans used housing policy for partisan purposes. George W. Bush publicly set a goal of 5.5 million more minority homeowners, and backed that up with the American Dream Downpayment Act of 2003, which subsidized first time purposes by low income buyers. Despite this, and unlike the Democrats, the Republicans sought a market based policy that would reward their campaign contributors with lavish profits. A series of well publicized events in 2001 showcased the head of the Office of Thrift Supervision (OTS), which is one of several federal government regulators of savings banks (i.e. *sparkassen*), and the Federal Deposit Insurance Company (FDIC) using a chainsaw to cut through a stack of regulatory manuals with the help of representatives of bank lobbying associations. Lenders regulated by OTS began originating and securitizing a vastly expanded volume of subprime loans, as well as a vastly expanded and increasingly risky range of mortgage products. Thus, for example, OTS supervised banks originated about \$255 billion in so-called Option ARM loans in 2006, which amounted to one-sixth of the entire stock of subprime loans at the time the crisis hit (Appelbaum and Nakashima, 2008). In an Option ARM, the borrower is free to reduce his payment in any given month and have the shortage added to the principal of the mortgage debt. These borrowers were thus vulnerable to both the risk that interest rates might rise (because the loan was an ARM, or adjustable rate mortgage), as well as the risk that their payment would rise to amortize the new, larger principal. Banks could market Option-ARMs, and ARMs in general, as having very low ‘teaser’ interest rates to customers whose income was too low to qualify them for a prime or conforming Fannie Mae mortgage. On the other side, the Bush administration pressured Fannie Mae and Freddie Mac to securitize more subprime mortgages as a way of rescuing increasingly troubled private mortgage originators.

Similarly, the Bush administration made a conscious decision in 2005 not to regulate the rapidly proliferating non-depository financial institutions that were originating the bulk of the subprime and Alt-A

(intermediate between prime and subprime) loans, even though voices in the Office of the Comptroller of the Currency (OCC – another bank regulator) and the Federal Reserve were warning that rising defaults on these loans posed a considerable threat to the financial system (Gramlich, 2007). The pattern of subprime lending explains part of this non-decision. Subprime lending was concentrated in areas rich in presidential electoral votes as well as rich in poor minority voters. Latinos account for at least 30 percent of the electorate in Arizona, California, Texas and New Mexico, 25 percent in Nevada, and 20 percent in Florida. By 2006, roughly one half of all mortgages made to blacks and latinos were in the subprime categories. Nevertheless, Fannie Mae estimated that roughly half of those subprime loans could have qualified for lower interest rate prime or near prime loans (Squires and O'Connor, 2001).

The flood of easily available, but expensive, mortgage money these policies made possible easily exceeded that of the Clinton administration, but with more modest results. Under Clinton, subprime originations rose from \$65 billion in 1995 to \$138 billion in 2000, and produced an increase in homeownership rates of 3.4 percentage points (Chomsisengphet and Pennington-Cross, 2006: 37). Under Bush, subprime originations rose to \$332 billion in 2003 and then peaked at \$625 billion in 2006 and increased their share from 8.6 percent to 20 percent of originations.<sup>4</sup> But this produced only an additional 1.6 percentage point gain in homeownership before round-tripping back down to the Clinton era level. Among blacks, the 5.1 percentage point increase under Clinton was succeeded by a temporary 2.1 percentage point gain under Bush. Only among latinos did a similar 5.1 percentage point gain give way to a more durable 2.8 percentage point gain (Harvard JCHS 2009:37). These gains came at an extremely high macroeconomic cost. Unlike the more sustainable Clinton boom, where rising incomes validated house price increases, the flood of mortgage money in the 2000s caused house prices to rise unsustainably (Schwartz, 2009b). From 2000 to 2007 the ratio of the median price for owner-occupied housing to median family income rose from 2.4 to 3.2 – a 32 percent jump – across the entire United States. But these increases were even greater in the politically salient states: 108 percent to 8.3 for California, 84 percent to 5.1 for Nevada, 64 percent to 4.2 for Arizona, and 83 percent to 4.2 for Florida (Lucy and Herlitz, 2009). Unsurprisingly, these states led the pack in terms of the percentage of homes in foreclosure in 2008, with California, Florida, Nevada, and Arizona accounting for 62 percent of all foreclosures that year.

### 3d: The crisis

The fundamental problem with the deregulated provision of mortgage credit was that lenders and borrowers alike made decisions that could only be validated through continued 10 percent annual housing price appreciation. Seventy-eight percent of all subprime mortgages originated in 2006 were 2/28 ARMs, that is, 30 year mortgages with a low introductory rate that would reset to the market rate after two years, and 92 percent were some kind of ARM. The typical subprime ARM in 2007 was resetting from about a 7 or 8 percent annual interest rate to something closer to 10 or 11 percent. The typical Alt-A buyer, with good credit but an excessively large loan in relation to incomes, was in much the same position, as 68 percent of these loans were ARMs (Credit Suisse, 2007b: 4-5, 19-21). Subprime and Alt-A borrowers were betting that continuously rising housing prices would bail them out of their ARM before the first, crippling interest rate reset. If housing prices continued to rise 10 percent or more annually, then after two years our erstwhile subprime borrower would find themselves with 20 percent equity in their house and qualify for a lower fixed interest rate, conforming 30 year mortgage. While this gamble paid off in the early years of the Bush administration, housing prices stopped rising after 2005. Thus, where only 4 percent of all 2004 vintage securitized subprime loans were in default after nine months, 10 percent of 2006 vintage loans and 16 percent of 2007 vintage subprime loans were in default after nine months.

This should not be surprising. The central problems faced by the bottom 20 or 30 percent of the income distribution are insufficient and erratic income, and thus an inability to surmount any financial or health risk. As of 2006 – before food and fuel prices really shot up – 20 percent of homeowners (homeowners, not households) in the bottom half of the income distribution were already spending more

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<sup>4</sup> By contrast, the total volume of securitized mortgages in Europe for 2005 was roughly €326 billion, and the cumulative volume 2000-05 was roughly €1072 billion, versus a cumulative \$1690 billion in securitized subprime and Alt-A mortgages and \$6691 billion in securitized prime mortgages in the United States (Aalbers, 2009a:402-3; Schwartz 2009:103).

than half their income on housing. A further 19 percent were spending between 30 and 50 percent of their income on housing. All together, 30 percent of all homeowners were spending more than 30 percent of their income on housing as did 20 percent of all US households, including renters (Harvard JCHS, 2008; Credit Suisse, 2007a: 26). In this situation, any income shock – rising gasoline prices, more expensive food, shorter work hours, illness, an interest rate reset – is enough to tip a family into default.

In this respect housing policy under both Clinton and Bush did not address the fundamental problem: housing wealth is no substitute for a robust system of risk sharing across the life cycle, across classes and across generations. Instead, housing policy aggravated those risks, although the lion's share of blame for the financial crisis surely falls on the investment banks that dispersed bad subprime and Alt-A mortgages through the entire financial system in the form of Collateralized Debt Obligations. One consequence is that housing finance has effectively become renationalized and reregulated. The crisis has effectively destroyed US private issuers of MBS; private MBS issues declined to zero in the third quarter of 2007. Most private securitizers were or are in bankruptcy. This leaves only the government sponsored enterprises – Freddie and Fannie plus the Federal Home Loan Banks – standing as large scale purchasers of raw mortgages and producers of credible MBS. In the last half of 2007, these three institutions generated nearly all of the new credit in the US housing market. The FHLBs supplied capital to mortgage lenders on the one side, while Fannie and Freddie absorbed and packaged mortgages on the other side. The re-emergence of the Frannies constitutes a re-nationalization of US housing finance. Outside the United States, efforts to legalize and expand securitization are now in abeyance. This reinforces the existing complementarity between public PAYGO pensions and low rates of homeownership.

The crisis of course also comes with a variety of human costs. Homelessness has risen in the United States, though by much less than European observers might expect given a 5 percentage point increase in unemployment. About 1.4 million people experienced at least one night of homelessness during the year in 2008. Half of these were in four states with the highest rates of foreclosures, and more than half were minorities (HUD, 2009). Nevertheless, the United States avoided a huge surge in homelessness during the financial crisis for three reasons. First, during 2007-09 banks forbore from foreclosing on all loans in default. They lacked the capacity to process that many foreclosures and correctly feared that they would drive down prices for their collateral by flooding the market with extra supply. Second, the population being evicted from foreclosed houses differed markedly from the usual homeless population. Most had sufficient social and familial ties to “double-up,” increasing crowding but not homelessness. Third, the US had an oversupply of housing, and many owners of investment properties chose to drop rents rather than have zero cash flow.

#### 4: Conclusion: housing, housing finance and welfare

Housing was the weak pillar of the welfare state and of the welfare state literature. In the formative years of the post-world war II welfare state, widespread homeownership appears to have been one factor limiting the potential political coalition pushing for a broad, public, second tier pension in some countries. As Castles argues, property generated a kind of pension income, albeit unevenly distributed. But this dynamic began to break down in the 1960s, as a range of state policies everywhere facilitated the gradual expansion of homeownership that most people seemed to favor. The welfare state literature, however, focused its attention on its traditional menu items – unemployment insurance, social assistance, and government supplied services – rather than asking what broad homeownership might imply for the welfare state. During the 1980s and 1990s, welfare re-organization got serious and even highly socialized systems like Sweden began to introduce more market mechanisms (Schwartz, 1994). The increasing individuation of risk in the liberal economies forced people to rely even more on homeownership as a substitute for social risk sharing mechanisms. Yet at the same time, states were deregulating mortgage finance, breaking down the walls between mortgage finance and the rest of the financial system, and either creating or expanding financial firms' ability to securitize mortgages. These two trends collided in the mid-2000s, with traumatic consequences for financial firms and would-be homeowners alike.

To put the main point bluntly: if the welfare state did bring capitalism to its knees, it was not through continual expansion of the tax and spend side of the welfare state, as many had feared. Rather, continual efforts to rollback the welfare state through marketization of the public sector and increased

commodification of housing created the crisis. Lech Walesa, an electrician, once remarked that he had never broken a screw putting one in, but had broken many screws trying to take them out. The same is true of neo-liberal efforts to 'reform' the connection between the welfare state and housing by creating markets for financial assets tied to housing, and by encouraging people to treat their houses as an asset. These recommodifying reforms enlarged the already large proportion of housing debt in specific countries' financial systems. Housing often represents the single largest asset (and liability) for most people, and housing related debt often represents one of the largest asset categories in most financial systems. In highly stratified and securitized housing finance systems, access to this housing wealth enabled excessive consumption via increased debt. Enlarging and deregulating housing finance thus made it possible for a crisis in housing markets and housing finance markets to trigger a major crisis for capitalism. Financialization of the housing sector was not the only reason for the current crisis, but it was certainly a major factor. Efforts to unscrew the welfare state, to separate individuals from their social rights, and to turn dwellings into consumable assets for partisan purposes also helped break the financial system by creating unsustainable levels of mortgage debt. It remains to be seen if it breaks the pension system as well, because so many assets are tied up in mortgage backed securities and the financial firms that generate them.

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