November 3, 2011

The **Yid with Lid** blog posts on what Bush understood about the Middle East that his successor does not.

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After three years of a very slow learning curve there are still things about the Middle East that George Bush understood and Barack Obama doesn't get.

King Abdullah of Jordan, a long-time ally of the US told the Washington Post's Lally Weymouth that Obama has a lot to learn about being an ally, and seemed to indicate that the United States is no longer trusted in the Muslim Middle East:

***Weymouth**: It is astounding that Tantawi [head of Egypt's military ruling council] did not take President Obama's call for hours the night the Israelis were trapped in their embassy in Egypt.*

***Abdullah**:The feeling I got from the Egyptian leadership is that if they stick [their] necks out, they will just get lambasted like [former president Hosni] Mubarak did. So I think they are playing safe by just keeping their heads down, which I think .□.□. sometimes allows things to get out of control. .□.□. Tantawi thinks there is too much pressure on him. ...*

... Unlike Bush, Obama does not seem to understand the strategic value of our most solid ally in the Middle East. Even worse, he gives no support to Israel and instead sides with a Palestinian Government who does anything it can to avoid making peace. He bashes Israel but when the PA was not responding to Israel's ten-month-long freeze on building within existing settlements he was silent; in October 2009, when the PA rejected Obama's plea for intense talks to be held in Washington he was silent, and even last week when Mahmoud Abbas said I've said it before, and I'll say it again: I will never recognize the Jewishness of the state, or a 'Jewish state," Obama is silent

It has been three years since Barack Obama was elected the president who was going to "repair" our relationship with the world, instead he has hurt our relationship with our strongest allies in the Muslim Middle East while attacking Israel, a strategic partner who has helped us with insights and technology to fight the war on terror.

Michael Rubin says the Kurds in Iraq have figured us out.

The Iraqi Kurds have prided themselves on being America's allies throughout the Iraq war and its aftermath. Repeatedly, regional leader Masud Barzani told visiting American generals and dignitaries that the Kurdish region was the most pro-American in Iraq.

The Kurdish authorities, however, have never made ideological alliances, but are the ultimate realists: Barzani forms partnerships with whomever he believes can most fulfill his own interests. With the U.S. withdrawal from Iraq, it is clear that anyone with an ounce of self-preservation is rushing to cut deals with the Iran. After all, the most common Iranian influence theme, Iraqi *politicians say, is that "You may like the Americans better, but we will always be your neighbors." Hence, on October 29, Barzani traveled to Iran where, on Sunday, he warmly embraced both Iranian President Mahmoud Ahmadinejad, and Supreme Leader Ali Khamenei. According to press reports, Barzani declared, "We will not forget the assistance of the Iranian people and government during the hard times passed by Iraq. To preserve our victory we need Iranian assistance and guidance…."*

Everyone in the region knows that the way Iraqis negotiate is to state extreme positions as a deadline approaches, and then go behind closed doors in a smoke-filled room to hash out agreements. The Iranians often quip that they play chess while the Americans play checkers. No one expected Obama to forfeit before the game actually began. But, alas, now that he has done so, he will discover just how deeply he has lost Iraq and Iraqis.

David Harsanyi says if you want more equality, you need more capitalism.

... You will notice that the Occupy Wall Street crowds -- and the progressives who support them -- focus on bringing the wealthy down to earth rather than lifting the 99 percent. They have a nearly religious belief that too much wealth is fundamentally immoral and unhealthy for society. The economic systems they cheer on would coerce downward mobility for the sake of equality but ignore prosperity for the people they claim to represent.

If progressive were interested in mitigating inequality, they would support the dynamism of free markets to allow the merit of ideas, products and services to win the day rather than stifle companies and pick winners in the name of imagined "progress." Yes, "too big to fail" means banks, but it also means union-backed bureaucracies, political parties, car companies and green energy -- and more.

If they were interested in spreading wealth, they would support lifting barriers that inhibit markets and make life difficult for entrepreneurs and businesses rather than spreading the destructive notion that life can only be "fair" if we rely on dependency and entitlement and tear down those who have more.

A week ago, a great piece appeared in the **Wall Street Journal** with more background on the credsis. We continue to believe it is important to understand the origins of this crisis. Here we learn how middle management at Freddie Mac was pushing back against the lowering of standards.

Occupy Wall Street is denouncing banks and Wall Street for "selling toxic mortgages" while "screwing investors and homeowners." And the federal government recently announced it will be suing mortgage originators whose low-quality underwriting standards produced ballooning losses for Fannie Mae and Freddie Mac.

Have they fingered the right culprits?

There is no doubt that reductions in mortgage-underwriting standards were at the heart of the subprime crisis, and Fannie and Freddie's losses reflect those declining standards. Yet the decline in underwriting standards was largely a response to mandates, beginning in the Clinton *administration, that required Fannie Mae and Freddie Mac to steadily increase their mortgages or mortgage-backed securities that targeted low-income or minority borrowers and "underserved" locations.*

The turning point was the spring and summer of 2004. Fannie and Freddie had kept their exposures low to loans made with little or no documentation (no-doc and low-doc loans), owing to their internal risk-management guidelines that limited such lending. In early 2004, however, senior management realized that the only way to meet the political mandates was to massively cut underwriting standards.

The risk managers complained, especially at Freddie Mac, as their emails to senior management show. They refused to endorse the move to no-docs and battled unsuccessfully against the reduced underwriting standards from April to September 2004. Here are some highlights: ...

Streetwise Professor on Jon Corzine's fall.
FCM, investment bank, primary dealer, and wanna be Goldman MF Global declared bankruptcy today. As is typical with financial firms, the end came quickly. The firm's problems metastasized quickly last week. Another quarterly loss, a ratings downgrade, and worries about losses on trades in European government bonds led to the typical downward spiral of lost funding and lost customers. These firms are very fragile. When they fall, they usually don't get up.

Ironically, MF's FCM operation was acquired from . . . REFCO, which cratered almost exactly 6 years ago, in October, 2005. Will anyone dare to take on this cursed franchise?

Piecing things together, I surmise that the firm bought about $6 billion in Italian and other southern Euro bonds and repo'd them out. Due to the decline in the prices of these bonds, and the firm's deteriorating financial condition, the repo counterparties demanded higher haircuts. The firm couldn't come up with the cash, and in desperation maxed out its credit lines. But that couldn't stop the hemorrhaging.

The most likely explanation for all this is that the firm was already foundering, and CEO John Corzine tried to gamble on resurrection by ramping up the risk. As is so often the case, this more often results in a more rapid descent to financial hell than resurrection.

One major irony is that MF Global was pushing hard for low capital requirements for members of OTC derivative CCPs. How's that idea looking now, GiGi?

Especially since suspicions are rife that MF has misused segregated customer funds, presumably to keep the resurrection gamble going. Reports state that the firm is stonewalling regulators on turning over records, and that about $300 million in customer funds are missing. This is one of the most egregious things a brokerage firm can do.

This is already a major fall for former Goldman CEO, US senator, and NJ governor Corzine. He is also a major Obama fundraiser, who is presumably now a Nonperson. If the suspicions about misuse of customer funds prove true, major fall won't even come close to describing what lies in store for Mr. Corzine. He will long to be merely a Nonperson.

On the news Jon Corzine's firm mixed customer and firm accounts, Contentions' **Seth Mandel** says;

... Stanford business professor Darrell Duffie told Bloomberg: "It's kind of considered the third rail of the brokerage industry that when you're holding your customers' funds in their names, you don't touch them — even in an emergency situation when you're running short of cash."

It's not only the third rail, it's common sense. But an executive who has already bet many millions of his firm's dollars on the prospect that President Obama was going to toss him a cushy federal appointment is probably not being too careful about other people's money.

Corzine is one of the Obama re-election campaign's major "bundlers," and he hosted a fundraiser to shower the Obama campaign with Wall Street cash several months ago. One expects his federal appointment to be abandoned rather quickly now, and Corzine's political future is probably over as well. Residents of New Jersey now have yet another reason to be happy they voted Corzine out of office in favor of Chris Christie in 2009. Corzine's political career was devastating for the state. ...

Michael Barone calls attention to an important vote on taxes in Colorado.

While Washington was transfixed by the evolving responses of Herman Cain to the unfolding sexual harassment story and the financial press was transfixed by the sudden decisions of the Greek government to hold a referendum on the current (evolving?) bailout settlement and to fire the heads of all the military services, Coloradans went to the polls and voted on Proposition 103, championed by Boulder state Senator Rollie Heath, which would have raised the state income tax from 4.63% to 5% and which was marketed as a way to aid teachers and kids. Democratic Governor John Hickenlooper, elected with 51% in 2010 against split opposition, stayed neutral. Voters weren't: they voted 64%-36% against 103.

The county by county returns provide an interesting insight on which Democratic constituencies backed the tax increase. ...

...Relevance for 2012? Well, Obama strategists have pointed to Colorado as the model for a state they hope to carry again--relatively high income, high education--and it voted 54%-45% for Obama in 2008. The results for the university towns and the skitopias bode well for him. The results from the rest of the state don't.

In the above piece, Barone refers to a post by Megan McCardle that linked to a fascinating blog post on the two tiers of new elites in the country. That post was by **Kenneth Anderson** in Volokh Conspiracy. This wanders, but has the germs of interesting thoughts about the people involved in Occupy Wall Street.

Even more frightening is the young woman who graduated from UC Berkeley, wanting to work in "sustainable conservation." She is now raising chickens at home, dying wool and knitting knick-knacks to sell at craft fairs. Her husband has been studying criminal justice and EMT — i.e., preparing to work for government in some of California's hitherto most lucrative positions — but as those work possibilities have dried up, he is hedging with a (sensible) apprenticeship as an electrician. These young people are looking at serious downward mobility, in income as well as status. The prospects of the lower tier New Class semi-professionals are dissolving at an *alarming rate. Student loan debt is a large part of its problems, but that's essentially a cost question accompanying a loss of demand for these professionals' services.*

The OWS protestors are a revolt — a shrill, cri-de-coeur wail at the betrayal of class solidarity — of the lower tier New Class against the upper tier New Class. It was, after all, the upper tier New Class, the private-public finance consortium, that created the student loan business and inflated the bubble in which these lower tier would-be professionals borrowed the money. It's a securitization machine, not so very different from the subprime mortgage machine. The asset bubble pops, but the upper tier New Class, having insulated itself and, as with subprime, having taken its cut upfront and passed the risk along, is still doing pretty well. It's not populism versus the bankers so much as internecine warfare between two tiers of elites.

The downward mobility is real, however, in both income and status. The Cal graduate started out wanting to do "sustainable conservation." She is now engaged in something closer to subsistence farming.

Saturday night comes the biggest college football game of the year. Undefeated (#1) LSU travels to undefeated Alabama (#2). One month ago, the **WSJ ran an article** explaining how LSU had worked for a year to slim down their defense to prepare for Oregon who they defeated. While explaining the complexity of the Division One college game, the article closed with this caveat;

*... When the Ducks **(Oregon)** met LSU, they faced a fitter, faster and, in some instances, smaller defense than they'd seen on tape. It was, in some ways, a perfect doppelganger of their offense. After taking down the Ducks 40-27, LSU has since run its record to 5-0 **(Now 8-0)** and ranks No. 5 in the country in total defense in terms of yards allowed per play (3.8), while playing four ranked opponents. Those whippet-strong linemen—Mingo, Montgomery and Logan—lead the team with 4.5 tackles for loss and two sacks apiece. And 5-foot-9 cornerback Tyrann Mathieu leads the team with four forced fumbles and 25 solo tackles. (It's worth noting that Oregon has averaged 60.3 points in three wins since playing LSU.)*

If there's likely to be a reckoning for the skinnied-up Tigers defense, it might come on Nov. 5 when they head to Tuscaloosa to play Alabama. The Crimson Tide runs a conventional, pro-style offense from behind a jumbo-size line that averages 6 feet 4, 313 pounds. Those blockers, paired with 224-pound running back Trent Richardson, can make any defense look small.

Yid with Lid

What Bush Understood About The Middle East--Obama Still Doesn't Get

It was just about three years ago that America elected a president who was going to repair our relationship that was that he was going to "repair" our relationship with the world (especially the Muslim world) after eight years of that "cowboy" George "W" Bush. But three years into the Obama Presidency, our "relationship repairer-in-chief" has increased the divide between the US and the Muslim Middle East, while opening up a divide with Israel, a nation who continues to provide this country counter-terrorism, intelligence and technology useful in urban warfare.

After three years of a very slow learning curve there are still things about the Middle East that George Bush understood and Barack Obama doesn't get.

King Abdullah of Jordan, a long-time ally of the US told the Washington Post's Lally Weymouth that Obama has a lot to learn about being an ally, and seemed to indicate that the United States is no longer trusted in the Muslim Middle East:
Weymouth*: It is astounding that Tantawi [head of Egypt's military ruling council] did not take President Obama's call for hours the night the Israelis were trapped in their embassy in Egypt.*

Abdullah*:The feeling I got from the Egyptian leadership is that if they stick [their] necks out, they will just get lambasted like [former president Hosni] Mubarak did. So I think they are playing safe by just keeping their heads down, which I think .□.□. sometimes allows things to get out of control. .□.□. Tantawi thinks there is too much pressure on him.*

Weymouth*: From the streets?*

Abdullah*: No, from the West.*

Weymouth*: Do you and other leaders in this area believe you cannot rely on the U.S.?*

Abdullah*:I think everybody is wary of dealing with the West. .□.□. Looking at how quickly people turned their backs on Mubarak, I would say that most people are going to try and go their own way. I think there is going to be less coordination with the West and therefore a chance of more misunderstandings. Egypt is trying to develop its own way of moving forward.*
Obama never bothered to learn how the Middle East worked, instead he tried to impose his own vision upon the region. That vision led him to abandon allies such as Hosni Mubarak at the first sign of trouble, and to attack Libya without Congressional or public support. In the case of Egypt there is a strong possibility Obama helped ease out a dictator in exchange for rule by the oppressive Muslim Brotherhood, and the Libyan leadership seems to be chock full of al Qaeda.

The President also came up with his own vision of Israel. He sees the Jewish State a satellite nation of the United States, that must conform to his vision of peace. The Bush and even the Clinton administration saw Israel as a strategic ally who is on the front line in the battle against Islamist terrorism.

Writing in the Los Angeles Times, Robert Blackwill, deputy national security advisor for strategic planning in the Bush administration, and Walter Slocombe, undersecretary of defense in the Clinton administration laid out the strategic importance of Israel.
American leaders have traditionally explained the foundations of the U.S.-Israel relationship by citing shared democratic values and the moral responsibility America bears to protect the small nation-state of the Jewish people. Although accurate and essential, this characterization is incomplete because it fails to capture a third, crucial aspect: the many ways in which Israel advances U.S. national interests.
Today, Israeli contributions to U.S. national interests cover a broad spectrum. Through joint training, exercises and exchanges on military doctrine, the United States has benefited in the areas of counter-terrorism, intelligence and experience in urban warfare. Increasingly, U.S. homeland security and military agencies are turning to Israeli technology to solve some of their most vexing technical and strategic problems.

This support includes advice and expertise on behavioral screening techniques for airport security and acquisition of an Israeli-produced tactical radar system to enhance force protection. Israel has been a world leader in the development of unmanned aerial systems, both for intelligence collection and combat, and it has shared with the U.S. military the technology, the doctrine and its experience regarding these systems. Israel is also a global pacesetter in armored vehicle protection, defense against short-range rockets, and the techniques and procedures of robotics, all of which it has shared with the United States. (The full article is worth reading)
Three years into the Administration of Barack Obama the Muslim Middle East is going to hell in a hand-basket, or as my friend and teacher Barry Rubin said:
On February 11, or October 23, or November 28, 2011, the Middle East entered a new era. Whether you date it to the fall of Mubarak, the Tunisian election, or the Egyptian election, what do you think is going to happen in the next half-century in the region? This is now — I call it officially — the Era of Revolutionary Islamism.
Unlike Bush, Obama does not seem to understand the strategic value of our most solid ally in the Middle East. Even worse, he gives no support to Israel and instead sides with a Palestinian Government who does anything it can to avoid making peace. He bashes Israel but when the PA was not responding to Israel's ten-month-long freeze on building within existing settlements he was silent; in October 2009, when the PA rejected Obama's plea for intense talks to be held in Washington he was silent, and even last week when Mahmoud Abbas said *I've said it before, and I'll say it again: I will never recognize the Jewishness of the state, or a 'Jewish state,"* Obama is silent

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Contentions

Kurds May Be Barometers of Obama's Iraq Defeat

by Michael Rubin

The Iraqi Kurds have prided themselves on being America's allies throughout the Iraq war and its aftermath. Repeatedly, regional leader Masud Barzani told visiting American generals and dignitaries that the Kurdish region was the most pro-American in Iraq.

The Kurdish authorities, however, have never made ideological alliances, but are the ultimate realists: Barzani forms partnerships with whomever he believes can most fulfill his own interests. With the U.S. withdrawal from Iraq, it is clear that anyone with an ounce of self-preservation is rushing to cut deals with the Iran. After all, the most common Iranian influence theme, Iraqi politicians say, is that "You may like the Americans better, but we will always be your neighbors." Hence, on October 29, Barzani traveled to Iran where, on Sunday, he warmly embraced both Iranian President Mahmoud Ahmadinejad, and Supreme Leader Ali Khamenei. According to press reports, Barzani declared, "We will not forget the assistance of the Iranian people and government during the hard times passed by Iraq. To preserve our victory we need Iranian assistance and guidance…."

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Townhall

You Want More Equality? Support More Capitalism

by David Harsanyi

A person can't go but a few clicks on the Internet these days without tripping over some shocking item about the "explosion" of income inequality that has, like the dark smog of capitalistic excess, been choking the life out of this unjust nation. And when it comes to inequality, there is certainly only one vital question we must ask ourselves: Who cares?

If the wealthy get wealthier, no one has to become one penny poorer. This childish idea that the economy is a zero-sum game might appeal to the populist sentiments of the so-called 99 percent -- or to the envious nature of some others or to the emotions of many struggling through this terrible economy -- but in the end, it doesn't stand up to the most rudimentary inspection.

Not to mention, tales of runaway income disparity destroying the American middle class have been repeatedly debunked. James Pethokoukis at the American Enterprise Institute recently pointed out that new Congressional Budget Office "data show real median after-tax household income (half of all households have income below the median, and half have income above it) grew by 35 percent over the past three decades."

Over the past half-century, in fact, the wages of the middle class have captured a remarkably consistent share of gross domestic product. And the most important fact that eludes protesters and progressives is that the poorest 5 percent of Americans are still richer than nearly 70 percent of the world -- with a lot more opportunity to change that situation.

But let's concede that, thank goodness, some inequity will exist and will as long as we remain a largely meritocratic society. But even if corrosive disparity is tormenting us, as so many journalists would have you believe, how are we to fix it? Are Americans prepared to take on a massive social engineering project that entails politicians, commissars and czars making biased and arbitrary assessments about who deserves what and who doesn't? That sort of endeavor has been attempted to varying degrees of real economic tragedy. It's the sort of behavior that got us here.

What we should be worrying about is economic mobility. And we do well there, too. A 2007 Treasury Department study showed that 58 percent of households that were in the bottom quintile in 1996 moved to a higher level by 2005, and of households in the top 1 percent during the same time, more than 57 percent dropped to a lower income group. And economist Shikha Dalmia recently pointed to a study by the University of Chicago's Steven Kaplan that "shows that, despite government bailouts, in 2008 and 2009 the adjusted gross income of the top 1 percent -- a disproportionate number of whom work in the financial industry -- fell to 1997 levels."

These numbers show great mobility, upward and downward, and it's why "class" as a political wedge issue hasn't typically held traction -- though the Obama administration is doing its best to change that dynamic.

No doubt, the recent recession -- and "stimulus"-induced extension of that recession -- and structural and technological changes that often occur in the job market mean that every so often, we will have some painful times. Taking a snapshot of "inequality" when emotions are exacerbated by a recession is only meant to distort reality for political gain. And every time capitalism is hijacked by technocrats and bureaucrats, it seems there is a cry from other technocrats and bureaucrats (and their fellow travelers) to institute more of the top-down control that stifles mobility.

You will notice that the Occupy Wall Street crowds -- and the progressives who support them -- focus on bringing the wealthy down to earth rather than lifting the 99 percent. They have a nearly religious belief that too much wealth is fundamentally immoral and unhealthy for society. The economic systems they cheer on would coerce downward mobility for the sake of equality but ignore prosperity for the people they claim to represent.

If progressive were interested in mitigating inequality, they would support the dynamism of free markets to allow the merit of ideas, products and services to win the day rather than stifle companies and pick winners in the name of imagined "progress." Yes, "too big to fail" means banks, but it also means union-backed bureaucracies, political parties, car companies and green energy -- and more.

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WSJ

The Mortgage Crisis: Some Inside Views

Emails show that risk managers at Freddie Mac warned about lower underwriting standards—in vain, and with lessons for today.

by Charles Calomiris

Occupy Wall Street is denouncing banks and Wall Street for "selling toxic mortgages" while "screwing investors and homeowners." And the federal government recently announced it will be suing mortgage originators whose low-quality underwriting standards produced ballooning losses for Fannie Mae and Freddie Mac.

Have they fingered the right culprits?

There is no doubt that reductions in mortgage-underwriting standards were at the heart of the subprime crisis, and Fannie and Freddie's losses reflect those declining standards. Yet the decline in underwriting standards was largely a response to mandates, beginning in the Clinton administration, that required Fannie Mae and Freddie Mac to steadily increase their mortgages or mortgage-backed securities that targeted low-income or minority borrowers and "underserved" locations.

The turning point was the spring and summer of 2004. Fannie and Freddie had kept their exposures low to loans made with little or no documentation (no-doc and low-doc loans), owing to their internal risk-management guidelines that limited such lending. In early 2004, however, senior management realized that the only way to meet the political mandates was to massively cut underwriting standards.

The risk managers complained, especially at Freddie Mac, as their emails to senior management show. They refused to endorse the move to no-docs and battled unsuccessfully against the reduced underwriting standards from April to September 2004. Here are some highlights:

On April 1, 2004, Freddie Mac risk manager David Andrukonis wrote to Tracy Mooney, a vice president, that "while you, Don [Bisenius, a senior vice president] and I will make the case for sound credit, it's not the theme coming from the top of the company and inevitably people down the line play follow the leader."

Risk managers had already experimented with lower lending standards and knew the dangers. In another email that day, Mr. Bisenius wrote to Michael May (another senior vice president), "we did no-doc lending before, took inordinate losses and generated significant fraud cases. I'm not sure what makes us think we're so much smarter this time around."

On April 5, Mr. Andrukonis wrote to Chief Operating Officer Paul Peterson, "In 1990 we called this product 'dangerous' and eliminated it from the marketplace." He also argued that housing prices were already high and unlikely to rise further: "We are less likely to get the house price appreciation we've had in the past 10 years to bail this program out if there's a hole in it."

Donna Cogswell, a colleague of Mr. Andrukonis, warned that Fannie and Freddie's decisions to debase underwriting standards would have widespread ramifications for the mortgage market. In a Sept. 7 email to Freddie Mac CEO Dick Syron and others, she specifically described the ramifications of Freddie Mac's continuing participation in the market as effectively "mak[ing] a market" in no-doc mortgages.

Ms. Cogswell's Sept. 4 email to Mr. Syron and others also anticipated the potential human costs of the mortgage crisis. She tried to sway management by appealing to their decency: "[W]hat better way to highlight our sense of mission than to walk away from profitable business because it hurts the borrowers we are trying to serve?"

Politics—not shortsightedness or incompetent risk managers—drove Freddie Mac to eliminate its previous limits on no-doc lending. Commenting on what others referred to as the "push to do more affordable [lending] business," Senior Vice President Robert Tsien wrote to Dick Syron on July 14, 2004: "Tipping the scale in favor of no cap [on no-doc lending] at this time was the pragmatic consideration that, under the current circumstances, a cap would be interpreted by external critics as additional proof we are not really committed to affordable lending."

Sensing that his warnings were being ignored, Mr. Andrukonis wrote to Michael May on Sept. 8: "At last week's risk management meeting I mentioned that I had reached my own conclusion on this product from a reputation risk perspective. I said that I thought you and or Bob Tsien had the responsibility to bring the business recommendation to Dick [Syron], who was going to make the decision. . . . What I want Dick to know is that he can approve of us doing these loans, but it will be against my recommendation."

The decision by Fannie and Freddie to embrace no-doc lending in 2004 opened the floodgates of bad credit. In 2003, for example, total subprime and Alt-A mortgage originations were $395 billion. In 2004, they rose to $715 billion. By 2006, they were more than $1 trillion.

In a painstaking forensic analysis of the sources of increased mortgage risk during the 2000s, "The Failure of Models that Predict Failure," Uday Rajan of the University of Michigan, Amit Seru of the University of Chicago and Vikrant Vig of London Business School show that more than half of the mortgage losses that occurred in excess of the rosy forecasts of expected loss at the time of mortgage origination reflected the predictable consequences of low-doc and no-doc lending. In other words, if the mortgage-underwriting standards at Fannie and Freddie circa 2003 had remained in place, nothing like the magnitude of the subprime crisis would have occurred.

Taxpayer losses at Fannie and Freddie alone may exceed $300 billion. The costs of the financial collapse and recession brought on by the mortgage bust are immeasurably higher. Unfortunately, the Obama administration has perpetuated the low underwriting standards that gave us the crisis and encouraged the postponement of foreclosures by lending support to various states' efforts to sue originators for robo-signing violations.

Now they are trying to deflect blame from Fannie and Freddie by suing the originators who fulfilled the politically motivated demands of the government-sponsored agencies that drove the mortgage crisis. If successful, all of those efforts will further postpone the ability of banks to grow the supply of credit, and they will sow the seeds of the next mortgage bust.

Mr. Calomiris is a professor of finance at the Columbia Business School and a research associate of the National Bureau of Economic Research.

Streetwise Professor

MFers Go Bankrupt

by Craig Pirrong

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Contentions

The End of Corzine's Disastrous Career?

by Seth Mandel

Jon Corzine has made a career of risky bets, but it turns out his riskiest move was betting on himself. In August, Corzine–then chief of the commodities giant MF Global–sold investors debt, the interest on which Corzine promised would be raised one point if President Obama appointed him to a federal job.

It's exactly the kind of arrogance mixed with recklessness that got Corzine and his investors in the trouble that was revealed over the course of last week. First we learned that under Corzine's directorship, MF Global was going bankrupt because it purchased Europe's risky debt. Then several companies each expressed interest in buying parts of MF Global–only to find that the books were worse than they looked, and that no part of the company was salvageable. But yesterday's news was far worse. It turns out that $700 million of MF Global investors' money is missing, and the firm is being investigated to find out if Corzine skimmed investors' own money to cover his bets:

For now, there is confusion surrounding the missing MF Global funds. It is likely, one person briefed on the matter said, that some of the money may be "stuck in the system" as banks holding the customer funds hesitated last week to send MF Global the money.

But the firm has yet to produce evidence that all of the $600 million or $700 million outstanding is deposited with the banks, according to the people briefed on the matter. Regulators are looking into whether the customer funds were misallocated.

Stanford business professor Darrell Duffie told Bloomberg: “It’s kind of considered the third rail of the brokerage industry that when you’re holding your customers’ funds in their names, you don’t touch them — even in an emergency situation when you’re running short of cash.”

It’s not only the third rail, it’s common sense. But an executive who has already bet many millions of his firm’s dollars on the prospect that President Obama was going to toss him a cushy federal appointment is probably not being too careful about other people’s money.

Corzine is one of the Obama re-election campaign’s major “bundlers,” and he hosted a fundraiser to shower the Obama campaign with Wall Street cash several months ago. One expects his federal appointment to be abandoned rather quickly now, and Corzine’s political future is probably over as well. Residents of New Jersey now have yet another reason to be happy they voted Corzine out of office in favor of Chris Christie in 2009. Corzine’s political career was devastating for the state.

Having no interest in politics other than the power it granted him, Corzine’s gubernatorial term was marked by the state raiding taxpayers to reward Democratic interest groups. Businesses fled the state, as did residents who couldn’t afford the property taxes that are required to fund union bosses’ lavish benefits. The state’s educational institutions are a mess, since the recipients of Corzine’s contract negotiations–the teachers unions–were awarded the funds that should have gone to textbooks, computers, and after-school programs.

Corzine’s lack of policy understanding led to his giving every single proposed liberal regulation the green light, creating a situation in which the state’s red tape began devouring itself and making it impossible to do such things as build affordable housing for police officers and other safety officials. The state had actually ceased functioning on any meaningful level.

This latest scandal, however, may herald the end of Corzine’s career in politics and business. On the political front, at least, it’s about time.

Washington Examiner

Colorado votes against higher taxes

by Michael Barone

While Washington was transfixed by the evolving responses of Herman Cain to the unfolding sexual harassment story and the financial press was transfixed by the sudden decisions of the Greek government to hold a referendum on the current (evolving?) bailout settlement and to fire the heads of all the military services, Coloradans went to the polls and voted on Proposition 103, championed by Boulder state Senator Rollie Heath, which would have raised the state income tax from 4.63% to 5% and which was marketed as a way to aid teachers and kids. Democratic Governor John Hickenlooper, elected with 51% in 2010 against split opposition, stayed neutral. Voters weren’t: they voted 64%-36% against 103.

The county by county returns provide an interesting insight on which Democratic constituencies backed the tax increase. Not the white working class: Pueblo County voted 70% no and Adams County, which includes northern and eastern Denver suburbs with increasing Latin populations, voted 69% no. Denver County, coterimous with the central city, voted 54% no. The only counties voting yes were Pitkin (Aspen, 57% yes), Boulder (University of Colorado, 54% yes) and San Miguel (Telluride, 52% yes). Also casting higher than average percentages but less than 50% yes (this may not exhaust the list since not all the counties have reported results in my source) were Larimer County (Colorado State University) and counties that, like Pitkin and San Miguel, that I call skitopias (Summit, Eagle, Routt, Garfield, Gunnison, Ouray, Montezuma, La Plata). The skitopia counties have populations that consist of two groups, rich people who like to ski and can afford to live in the mountains and young people who serve them, working as waiters, store clerks, house cleaners, etc. These resemble the two groups described by the Atlantic's Megan McArdle in a characteristically fascinating and insightful (and long) blogpost.

So who's for higher taxes? On the one hand the university town people, living high off the higher education bubble for years but now afraid it may burst, and on the other hand the skitopia people, relatively indifferent to tax rates either because they're very rich or because they're too poor to pay taxes. The white working class and upwardly mobile Latinos join the exurbanites in Douglas County (67% no) and Elbert County (78% no, the highest in the state) in voting no. In other words, people who work for a living and pay taxes.

Relevance for 2012? Well, Obama strategists have pointed to Colorado as the model for a state they hope to carry again--relatively high income, high education--and it voted 54%-45% for Obama in 2008. The results for the university towns and the skitopias bode well for him. The results from the rest of the state don't.

Volokh Conspiracy

The Fragmenting of the New Class Elites, or, Downward Mobility

by Kenneth Anderson

Glenn Reynolds is correct in his weekend post to point to the social theory of the New Class as key to understanding the convulsions in the middle and upper middle class; I've written about it myself here at VC and in a 1990s law journal book review essay. The angst is partly income, of course — but it's also in considerable part, as Glenn notes, "characterized as much by self-importance as by higher income, and is far more eager to keep the proles in their place than, say, [Anne] Applebaum's small-town dentist. It's thus not surprising that as its influence has grown, economic opportunity has increasingly been closed down by government barriers."

The problem the New Class faces at this point is the psychological and social self-perceptions of a status group that is alienated (as we marxists say) from traditional labor by its semi-privileged upbringing — and by the fact that it is actually, two distinct strands, a privileged one and a semi-privileged one. It is, for the moment, insistent not just on white-collar work as its birthright and unable to conceive of much else. It does not celebrate the dignity of labor; it conceived of itself as existing to regulate labor. So it has purified itself to the point that not just any white-collar work will do. It has to be, as Michelle Obama instructed people in what now has to be seen as another era, virtuous non-profit or government work. Those attitudes are changing, but only slowly; the university pipelines are still full of people who cannot imagine themselves in any other kind of work, unless it means working for Apple or Google.

The New Class has always operated across the lines of public and private, however, the government-university-finance and technology capital sectors. It is not a theory of the government class versus the business class — as 1990s neoconservatives sometimes mistakenly imagined. As Lasch pointed out, it is the class that bridges and moves effortlessly between the two. As a theory of late capitalism (once imported from being an analysis of communist nomenkaltura) it offers itself as a theory of technocratic expertise first - but, if that spectacularly fails as it did in 2008, it falls back on a much more rudimentary claim of monopoly access to the levers of the economy. Which is to say, the right to bridge the private-public line, and rent out its access.

The OWS movement against this social theory backdrop? (Let's leave aside the material reality of its occupation, so far as one can tell today from shifting reporting: geographies in which public order was deliberately withdrawn to indulge a certain class of youth and not-so-youth (and the aging generation of New Class professionals projecting its political nostalgia onto it). The result is theft, violence, sexual assault, and levels of filth that, absent the infrastructure of the world's richest large society, would mean what it means in Haiti — dysentery, cholera, epidemic disease. Epidemic disease is what happens when you shit your nest, unless there is a larger society that will clean up after you. The culture industry averts its eyes in its effort to have its nostalgic dream intact. But leave that aside, and leave aside, too, the folks who send in the organic beet root and goat cheese — for the consumption of the wanna-be New Class that, somehow, has notions of property and entitlement of an intensity that only a born regulator can have, and therefore fine-tuned notions of who eats organic and who goes to the soup kitchen. This is further complicated by the confused politics of the protestors, engaging in confrontations with police, as Harry Siegel reports from New York, who seem to have responded by encouraging the homeless and disturbed to join them. Ann Althouse is right to point to Joan Didion's Slouching Toward Bethlehem, on the decline of the Haight-Ashbury utopia.)

In social theory, OWS is best understood not as a populist movement against the bankers, but instead as the breakdown of the New Class into its two increasingly disconnected parts. The upper tier, the bankers-government bankers-super credentialed elites. But also the lower tier, those who saw themselves entitled to a white collar job in the Virtue Industries of government and non-profits — the helping professions, the culture industry, the virtueocracies, the industries of therapeutic social control, as Christopher Lasch pointed out in his final book, *The Revolt of the Elites*.

The two tiers of the New Class have always had different sources of rents, however. For the upper tier, since 1990, it has come through its ability to take the benefits of generations of US social investment in education and sell that expertise across global markets — leveraging expertise and access to capital and technological markets in the 1990s to places in Asia and the former communist world in desperate need of it. As Lasch said, the revolt and flight of the elites, to marketize themselves globally as free agents — to take the social capital derived over many generations by American society, and to go live in the jet stream and extract returns on a global scale for that expertise. But that expertise is now largely commodified — to paraphrase David Swenson on financial engineering, that kind of universal expertise is commodified, cheaply available, and no longer commands much premium. As those returns have come under pressure, the Global New Class has come home, looking to command premiums through privileged access to the public-private divide — access most visible at the moment as virtuous new technology projects that turn out to be mere crony capitalism.

The lower tier is in a different situation and always has been. It is characterized by status-income disequilibrium, to borrow from David Brooks; it cultivates the sensibilities of the upper tier New Class, but does not have the ability to globalize its rent extraction. The helping professions, the professions of therapeutic authoritarianism (the social workers as well as the public safety workers), the virtuecrats, the regulatory class, etc., have a problem — they mostly service and manage individuals, the client-consumers of the welfare state. Their rents are not leveraged very much, certainly not globally, and are limited to what amounts to an hourly wage. The method of ramping up wages, however, is through public employee unions and their own special ability to access the public-private divide. But, as everyone understands, that model no longer works, because it has overreached and overleveraged, to the point that even the system's most sympathetic politicians understand that it cannot pay up.

The upper tier is still doing pretty well. But the lower tier of the New Class — the machine by which universities trained young people to become minor regulators and then delivered them into white collar positions on the basis of credentials in history, political science, literature, ethnic and women's studies — with or without the benefit of law school — has broken down. The supply is uninterrupted, but the demand has dried up. The agony of the students getting dumped at the far end of the supply chain is in large part the OWS. As Above the Law points out, here is "John," who got out of undergrad, spent a year unemployed and living at home, and is now apparently at University of Vermont law school, with its top ranked environmental law program — John wants to work at a "nonprofit."

Even more frightening is the young woman who graduated from UC Berkeley, wanting to work in "sustainable conservation." She is now raising chickens at home, dying wool and knitting knick-knacks to sell at craft fairs. Her husband has been studying criminal justice and EMT — i.e., preparing to work for government in some of California's hitherto most lucrative positions — but as those work possibilities have dried up, he is hedging with a (sensible) apprenticeship as an electrician. These young people are looking at serious downward mobility, in income as well as status. The prospects of the lower tier New Class semi-professionals are dissolving at an alarming rate. Student loan debt is a large part of its problems, but that's essentially a cost question accompanying a loss of demand for these professionals' services.

The OWS protestors are a revolt — a shrill, cri-de-coeur wail at the betrayal of class solidarity — of the lower tier New Class against the upper tier New Class. It was, after all, the upper tier New Class, the private-public finance consortium, that created the student loan business and inflated the bubble in which these lower tier would-be professionals borrowed the money. It's a securitization machine, not so very different from the subprime mortgage machine. The asset bubble pops, but the upper tier New Class, having insulated itself and, as with subprime, having taken its cut upfront and passed the risk along, is still doing pretty well. It's not populism versus the bankers so much as internecine warfare between two tiers of elites.

The downward mobility is real, however, in both income and status. The Cal graduate started out wanting to do "sustainable conservation." She is now engaged in something closer to subsistence farming.

WSJ

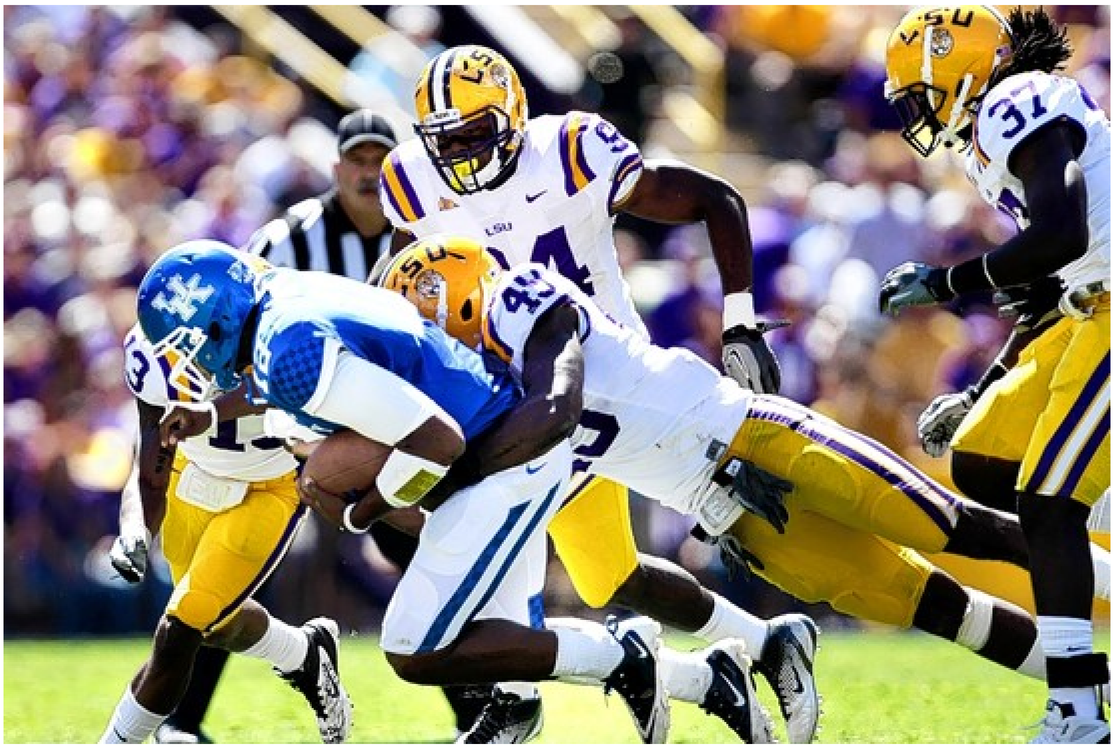
The Defense That Went to Fat Camp

Faced With a Brutal Schedule, No. 1 LSU Decided to Skinny Up its D; Fear and Plyometrics

by Scott Cacciola

Baton Rouge, La.

LSU has earned the country's No. 1 ranking in college football largely through the strength of its defense, which has treated opponents like piñatas this season, holding them to a sniveling two yards per rushing attempt. As LSU puts its unbeaten record on the line against No. 17 Florida this weekend, this unit is inviting comparisons to some of the all-time greats.



LSU defensive end Barkevious Mingo sacks Kentucky quarterback Morgan Newton during a game on Oct. 1.

But if you have any preconceptions about how a great Southeastern Conference defense gets made, you might want to set them aside. For one thing, this team's starting linemen and linebackers are rather small by the overfed standards of the SEC—they're about 20 pounds lighter, on average, than their equivalents at Alabama. But what really makes this defense unusual is the force that drove its development. It was built on fear—the fear of Oregon.

In September 2010, after LSU agreed to open the 2011 season against the Ducks, head coach Les Miles began to scheme—and sweat. Renowned for its up-tempo, spread-the-field offense and its flair for innovation, Oregon was a game-planning nightmare. (The only team to beat the Ducks last year was Auburn, which had six weeks to plot.) "You can't prepare for an uptempo style of play in one week," former Oregon coach Mike Bellotti said. "You can't do it in two weeks. It takes six weeks, minimum. If you can spend nine months on it, even better."

Miles and his staff recognized that losing to a PlayStation offense from the Pac-12 would be a tricky way to launch a season. But unlike many teams that have struggled to prepare for Oregon, LSU had a head start.

When LSU's defensive coordinator, John Chavis, arrived in 2009, he knew all about the Oregon menace. Defenses were being exposed by spread-type offenses that sprayed the ball to shifty playmakers in open spaces. Missed tackles were becoming the norm. Chavis said he knew he needed to recruit with care—and foresight. "The college game has gotten to be a speed game," he said. "If you don't have athletes who can run, you're in trouble."

When the Ducks showed up to play the Tigers on Sept. 3 at Cowboys Stadium, they faced a precocious defense. Two of LSU's top ends and its two starting tackles are sophomores. One of those ends, Barkevious Mingo, is a case study for the unusual thinking that went into this unit: At West Monroe (La.) High School, Mingo was a star sprinter capable of covering 400 meters in 48 seconds. He also was 6 feet 4, thin as a post, and hadn't played football until his junior year when the coach, Don Shows, convinced him to try out. "Big don't always mean good," Shows said. "We just lined him up and told him to get the guy who's got the ball. Nobody could block him."

The Mingo model was exactly what LSU's Chavis wanted: a defensive end who not only could pursue the quarterback but could also track quick backs and receivers when necessary. Mingo, who arrived on campus at 195 pounds, has since bulked to a listed 240.

Oregon's greatest weapon is relentlessness. The Ducks typically try to run a play every 18 to 22 seconds, a tempo that, according to Bellotti, is meant to "make those big defenders up front play with sloppy technique, make it so they can't focus and can't breathe." The damage often is most apparent late in games when defensive linemen—particularly the big tackles—are a step slower and more vulnerable to rushes up the middle.

LSU's four sophomore linemen—the ends Mingo and Sam Montgomery and defensive tackles Bennie Logan and Michael Brockers—were all red-shirted in 2009. This gave Tommy Moffitt, LSU's strength and conditioning coach, the chance—as he put it—to "experiment" with them.

Moffitt stressed plyometric training. He had them flip tires and push sleds, varying the resistance based on what he called the coefficient of friction. He charted how much each player moved at every practice, down to the yard. He went online and searched for new exercises, he said, until his "eyeballs bled."

One of Moffitt's favorite metrics is relative strength—a measure of how much work a player can do per pound of body weight. Defensive backs, he said, should score in the upper fives, defensive ends in the low fives and defensive tackles in the mid fours. If a player has a too-small number, Moffitt said, it's a sign that his "non-functional" mass is slowing him down.

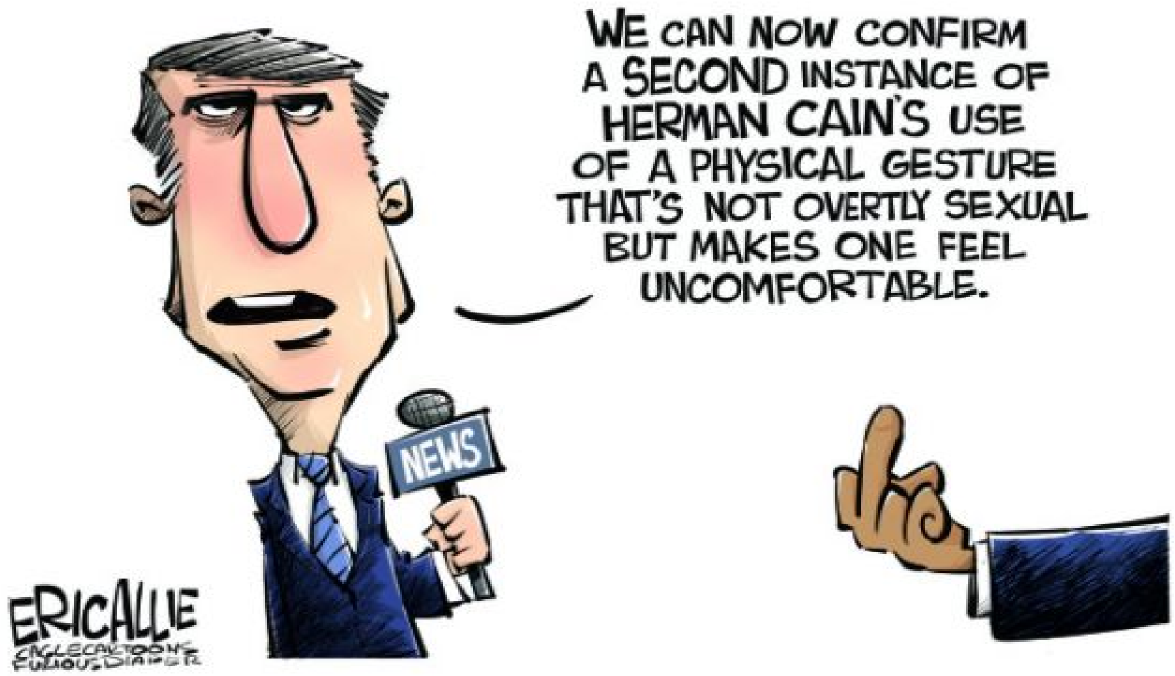
Moffitt believes that if a football player can lose 10 pounds while improving his relative strength, he'll be more efficient in games. "We're not going to roll a bunch of skinny minis out there on the field; that's not our goal," he said. "But we want every ounce of weight to be force-generating."

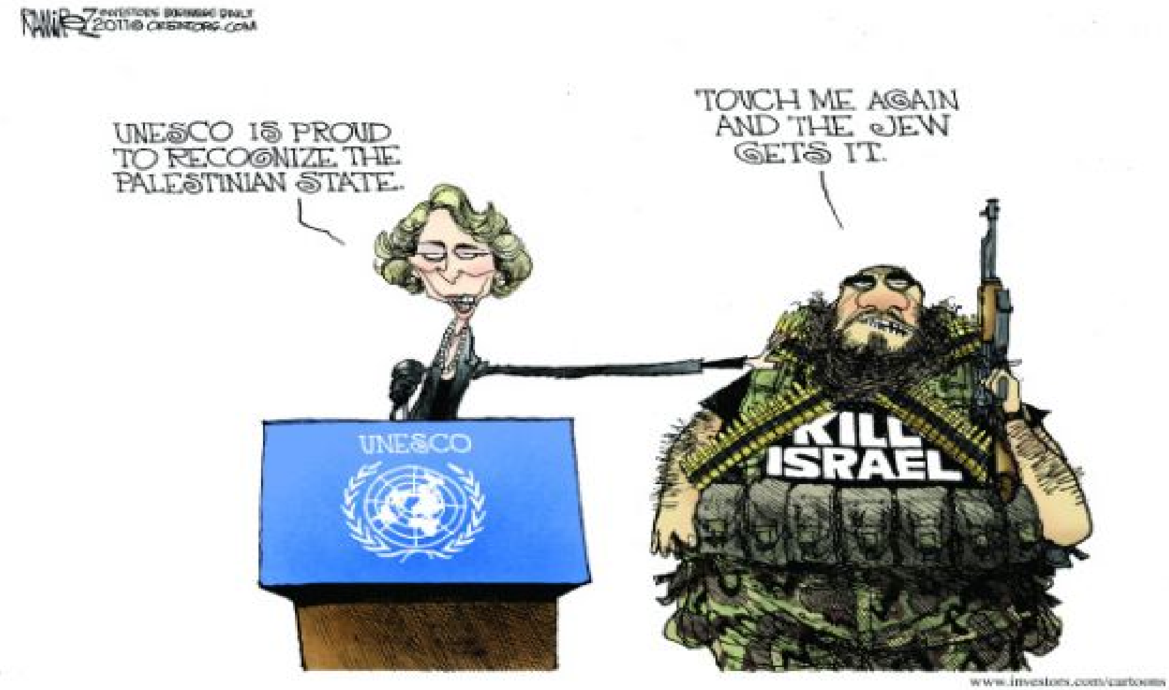
Brockers, the tackle, said it took some convincing for him to buy in. "I was afraid that I wouldn't have the strength or size" to take on 320-pound offensive linemen, he said. But after trimming down from 315 pounds to 305, he said he feels just as strong as he did last season—in addition to having more speed and stamina.

To simulate the rapid pace at which Oregon snaps the ball, Miles came up with a novel idea at spring practice: He had the defense work against two offenses. As soon as one offense finished running a play, a fresh new one trotted out. Miles liked it so much he carried it over to the preseason. "I want you to imagine practicing against a hurry-up Oregon offense in the middle of the summer," Montgomery said, "in *Louisiana*."

When the Ducks met LSU, they faced a fitter, faster and, in some instances, smaller defense than they'd seen on tape. It was, in some ways, a perfect doppelganger of their offense. After taking down the Ducks 40-27, LSU has since run its record to 5-0 and ranks No. 5 in the country in total defense in terms of yards allowed per play (3.8), while playing four ranked opponents. Those whippet-strong linemen—Mingo, Montgomery and Logan—lead the team with 4.5 tackles for loss and two sacks apiece. And 5-foot-9 cornerback Tyrann Mathieu leads the team with four forced fumbles and 25 solo tackles. (It's worth noting that Oregon has averaged 60.3 points in three wins since playing LSU.)

If there's likely to be a reckoning for the skinnied-up Tigers defense, it might come on Nov. 5 when they head to Tuscaloosa to play Alabama. The Crimson Tide runs a conventional, pro-style offense from behind a jumbo-size line that averages 6 feet 4, 313 pounds. Those blockers, paired with 224-pound running back Trent Richardson, can make any defense look small.

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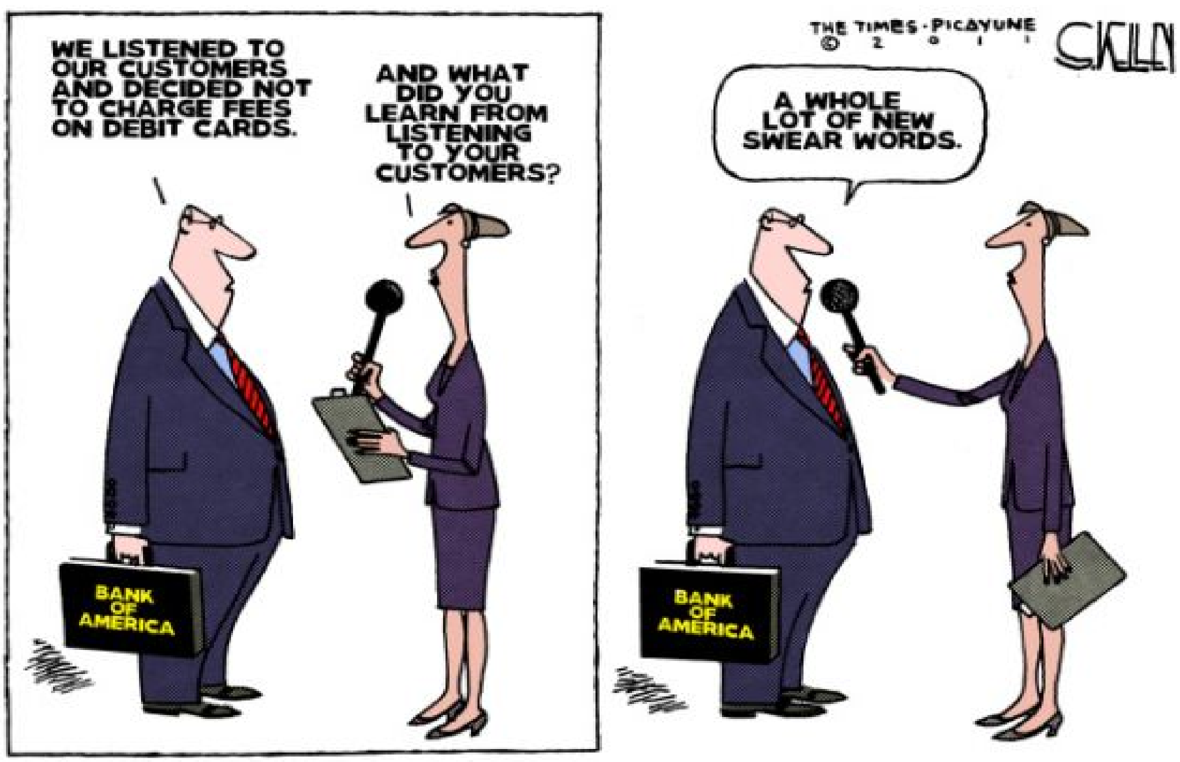
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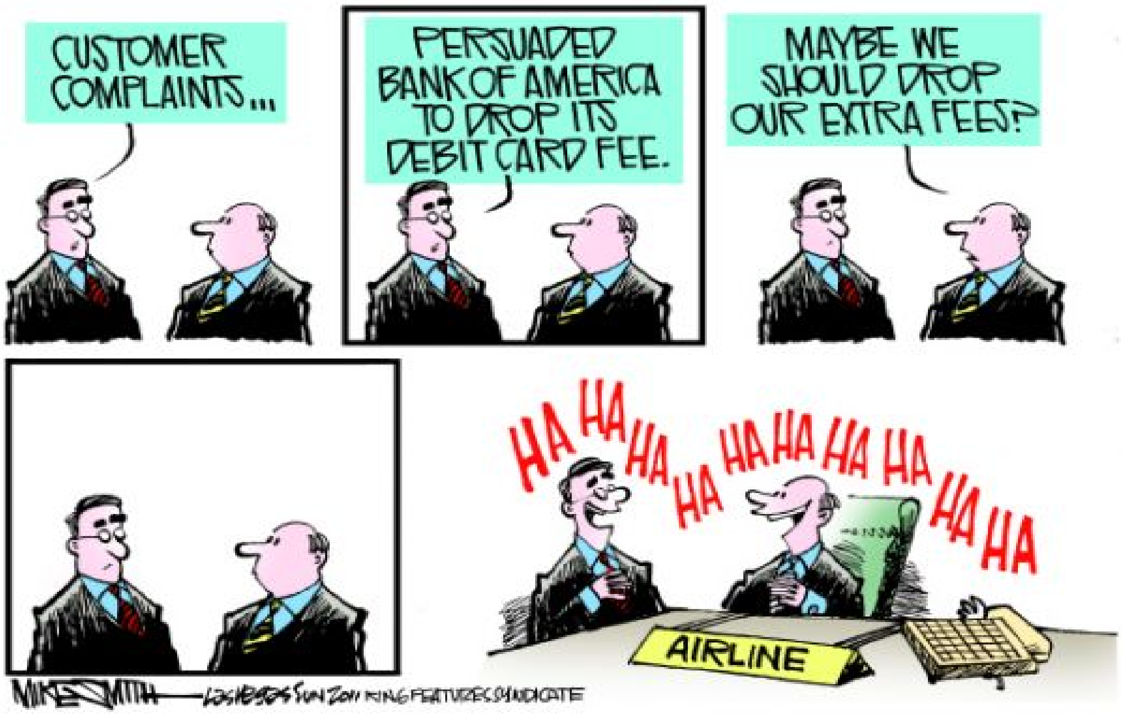
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