WEEK 3: The Financialization of Housing

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What is the Financialization of Housing?

What is Financialization?

- Financialization refers to “the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies” (Epstein, 2005 in Davis and Kim, 2015).
- Financialization of the global economy has meant increased outsourcing, a reorientation toward increasing shareholder profits, and reliance on the securitization (i.e., monetization) of debt (Davis and Kim, 2015) with mortgage debt being its dominant form backed by an ideology of homeownership (Aalbers, 2019).
- Assets, like housing more recently, are converted into tradable securities whereby credit risks are no longer fully borne by banks (Hudson and Bezemer, 2012).

What is Financialization?

As Bezemer and Hudson (2016) state,

“Mortgages are also special in that real estate assets have grown into the largest asset market in all western economies, and the one with the most widespread participation. Following classical analysis, if every real estate asset bought on credit skims off the income of the owner-borrower, then the rise in home ownership since the 1970s has sharply increased rent extraction and turned it into a flow of interest to mortgage lenders. Securitization added another dimension to this. Not only domestic homeowners, but also global investors can participate in the mortgage market” (p. 754).

What is Financialization?

Drawing on Lapavistas, Moreno (2014) defines three interlocking aspects of a financialized system as:

1. self-reliance of companies through seeking profits in the **sphere of circulation** (i.e. when money is transformed into a commodity and back into money) instead of through **fixed capital** (i.e. assets and investments used for production/to run a business)
2. commercial banks, behaving more like investment banks by facilitating speculative investment
3. real estate and housing, as sites that could "absorb masses of loanable-capital" (p. 253); (i.e. a "spatial fix")

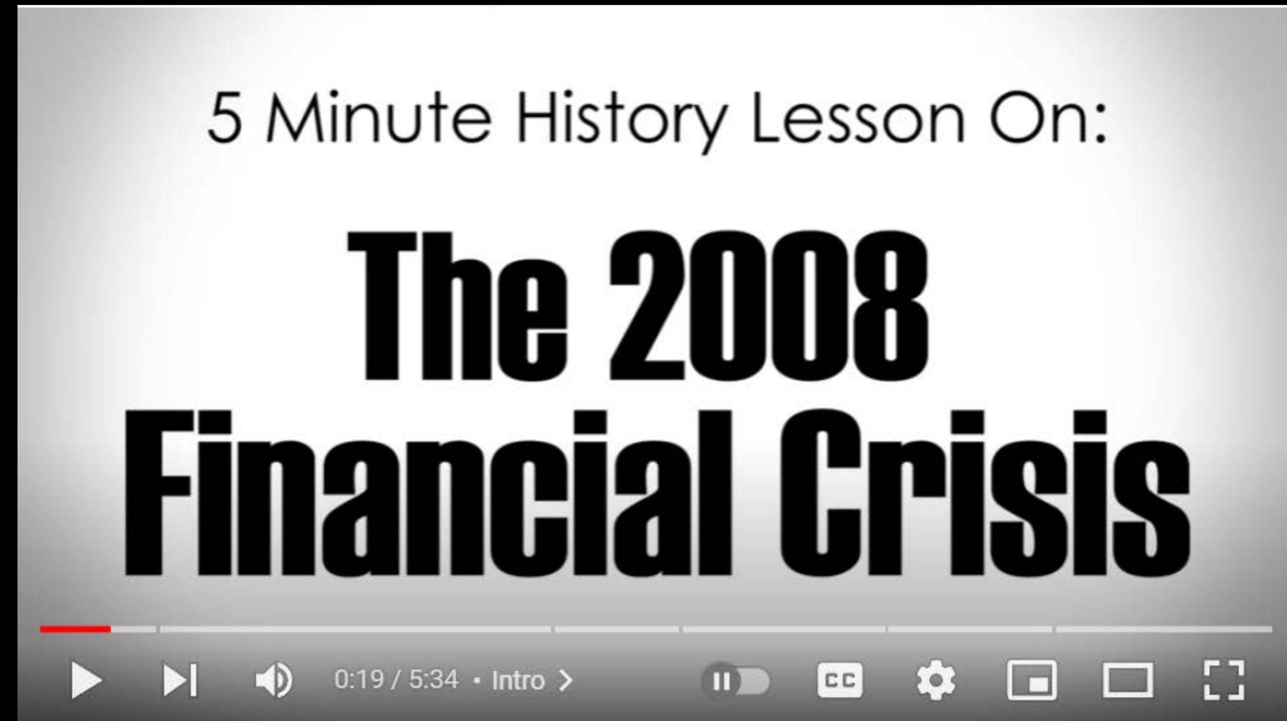
Real Estate as a "Spatial Fix" for Capital

Over the last 40-50 years, real estate has overtaken other forms of economic production (e.g. the making of goods), becoming the primary locus for a "spatial fix" (Harvey, 2006) for capital.

- Harvey (2001, p. 28) **The "spatial fix"** (in the sense of geographical expansion to resolve problems of overaccumulation) is in part achieved through fixing investments spatially, embedding them in the land, to create an entirely new landscape (of airports and of cities, for example) for capital accumulation.
- Jessop describes Harvey's **spatial fix** as: a general term that refers to many different forms of spatial reorganization and geographical expansion that serve to manage, at least for some time, crisis-tendencies inherent in accumulation.

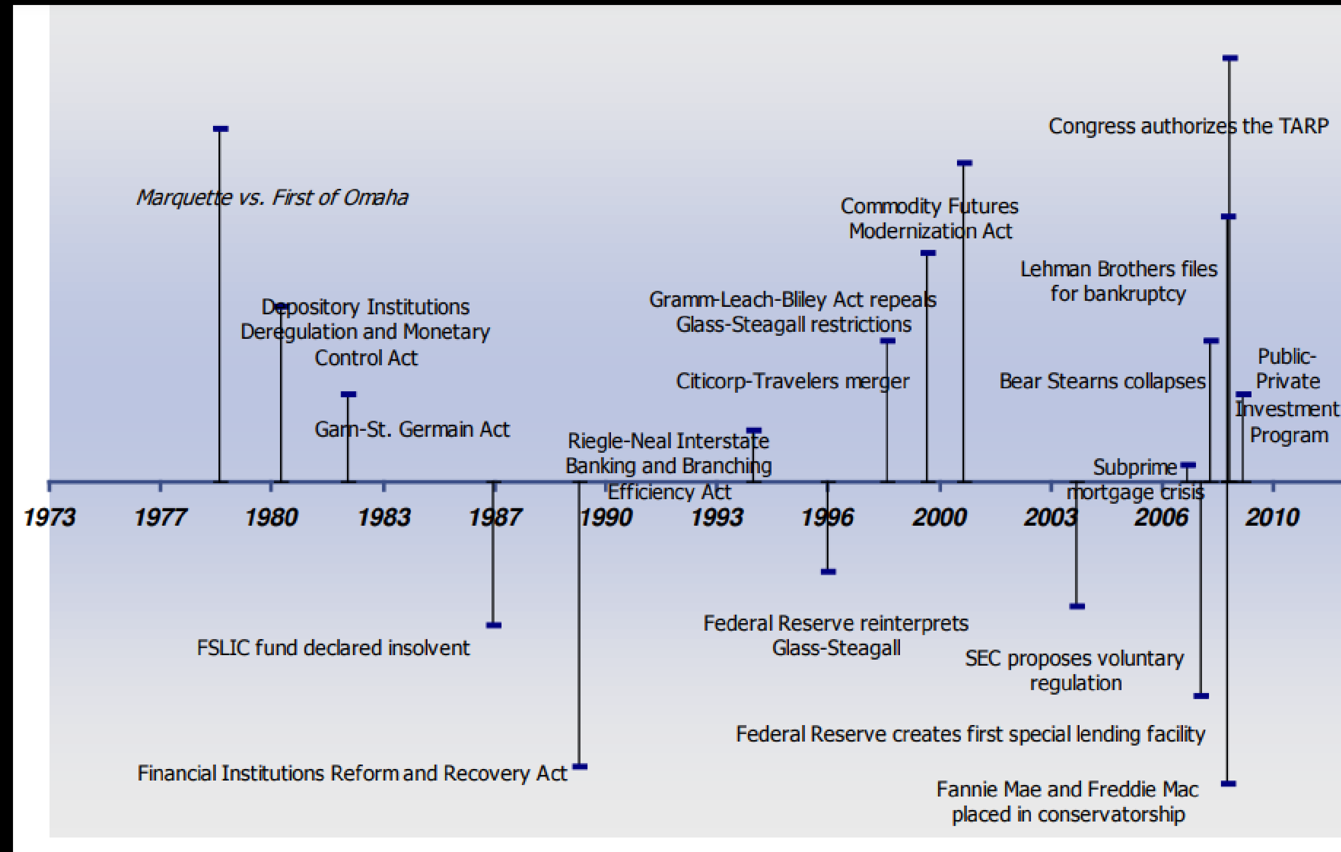
Financialization of the Economy: 2008 Crisis

- The 2008 Financial Crisis is a was caused by the increasing financialization of housing. whereby mortgages are treated like stocks and bonds, are pooled, and sold to investors.



Financialization of the Economy: Deregulation

- Since the Reagan Administration, the Federal Government's responsibility for providing affordable housing has devolved onto state and local entities using increasingly privatized means with a heavily deregulated banking system.



Sherman, M. 2009. "A Short History of Financial Deregulation in the United States". Center for Economic and Policy Research. [link]

Bank Deregulation

A history of **bank deregulation** can be found here (if you're interested!), but here are some key take-aways:

- **1978, Marquette vs. First of Omaha** – Supreme Court allows banks to export the usury laws of their home state nationwide and sets off a competitive wave of deregulation, resulting in the complete elimination of usury rate ceilings in South Dakota and Delaware, among others.
  - Per Wikipedia: Marquette Nat. Bank of Minneapolis v. First of Omaha Service Corp., 439 U.S. 299 (1978), is a unanimous U.S. Supreme Court decision holding that state anti-usury laws regulating interest rates cannot be enforced against nationally chartered banks based in other states.
  - Per americanbar.org: Usury laws are state-specific laws that set forth limits for interest rates in specific types of lending instruments to prevent lenders from imposing unreasonable or predatory interest rates

1996, Fed Reinterprets Glass-Steagall – Federal Reserve reinterprets the Glass-Steagall Act several times, eventually allowing bank holding companies to earn up to 25 percent of their revenues in investment (i.e. riskier) banking.

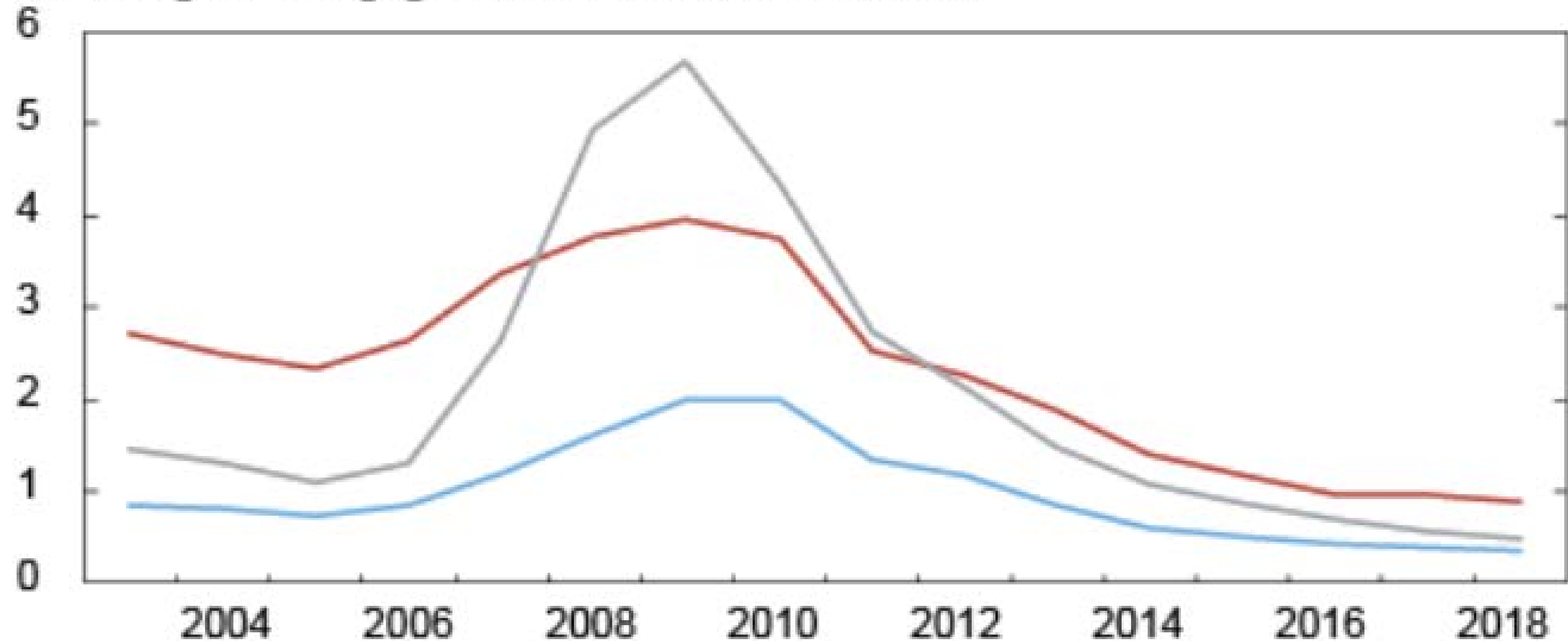
- Per https://www.federalreservehistory.org/: The Glass-Steagall Act effectively separated commercial banking from investment banking and created the Federal Deposit Insurance Corporation, among other things. It was one of the most widely debated legislative initiatives before being signed into law by President Franklin D. Roosevelt in June 1933.
- **1999, Gramm-Leach-Bliley Act** – With support from Fed Chairman Alan Greenspan, Treasury Secretary Rubin and his successor Lawrence Summers, the bill repeals the Glass-Steagall Act completely.
  - **2004, Voluntary Regulation** – The Securities & Exchange Commission proposes a system of voluntary regulation under the Consolidated Supervised Entities program, allowing investment banks to hold less capital in reserve and increase leverage.
  - **2007, Subprime Mortgage Crisis** – Defaults on subprime loans send shockwaves throughout the secondary mortgage market and the entire financial system.

- As the dominant form of debt, mortgage-backed securities have seemingly become synonymous with foreclosure.
- In the latter 20th century, increases in homeownership among African Americans was precipitated “by deregulatory policies that led to the rise of non-bank lenders, the proliferation of high-cost and exotic loan products, and the entry of banks into financial services previously reserved for investment banks” (Saegert et. al., 2011, p. 395). These factors along with surges in predatory lending and subprime loans, targeting minority families, led to widespread foreclosures across the country.

The Foreclosure Crisis Disproportionately Affected Zip Codes with a Majority of Black or Hispanic Residents

Majority white zip codes   Majority Black zip codes   Majority Hispanic zip codes

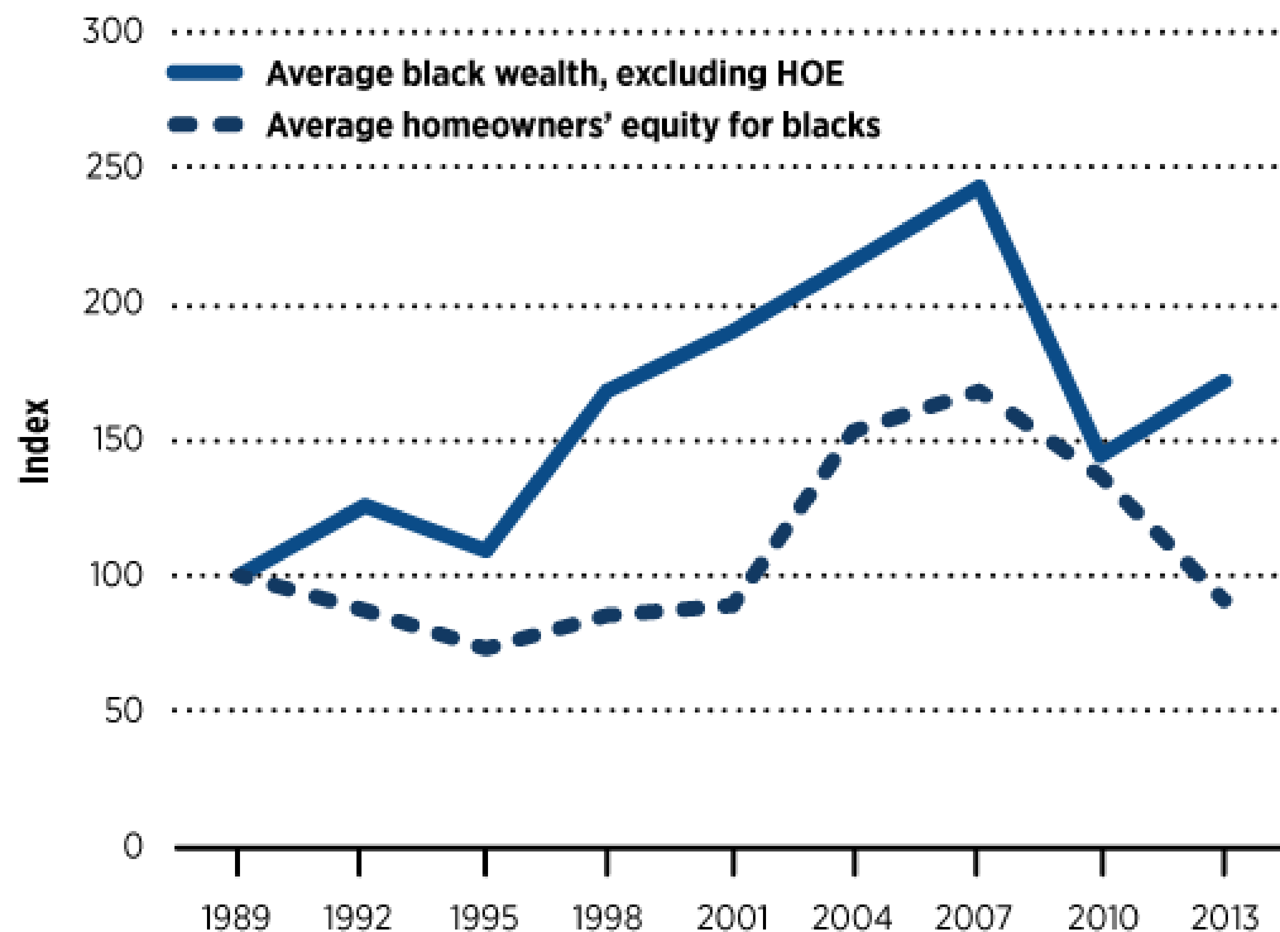
Percentage of mortgage-holders with new foreclosure



Sources: New York Fed Consumer Credit Panel / Equifax; U.S. Census Bureau.

FIGURE 2

Change in Average Wealth: Homeownership (HOE) vs. Other Assets for Blacks



SOURCE: Federal Reserve Board Survey of Consumer Finances (2013).
NOTE: The figure shows cumulative changes in the indexes (1989=100), adjusted for inflation.

■ FEDERAL RESERVE BANK OF ST. LOUIS

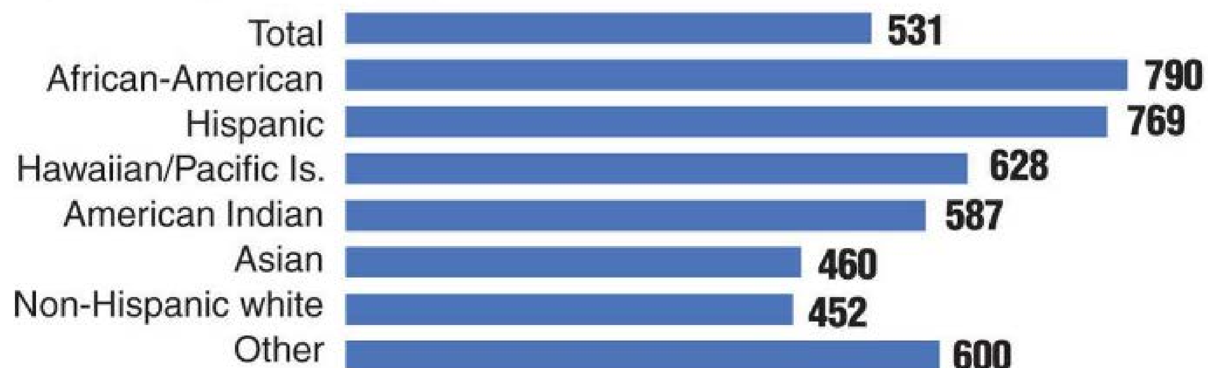
Demographics of foreclosure

How minorities have been disproportionately hit with home foreclosures:

In 2007-09, for mortgages originating in 2005-08

By racial, ethnic group

Per 10,000 home mortgages



By income group

		Percent of mortgages	Percent of Foreclosures	Increased likelihood of foreclosure than for non-Hisp. whites
Low	African-American	15%	21%	56%
	Hispanic	11%	12%	20%
	Non-Hispanic white	74%	67%	
Middle	African-American	10%	15%	71%
	Hispanic	13%	19%	67%
	Non-Hispanic white	77%	67%	
High	African-American	6%	10%	81%
	Hispanic	14%	23%	94%
	Non-Hispanic white	80%	67%	

Source: Center for Responsible Lending
Graphic: Judy Treible

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FIGURE 3A. TOTAL WEALTH VS. WEALTH EXCLUDING HOME EQUITY: WHITE HOUSEHOLDS

$300,000
$250,000
$200,000
$150,000
$100,000
$50,000
$-

1999 2001 2003 2005 2007 2009 2011

Wealth Including Home Equity
Wealth Excluding Home Equity

FIGURE 3B. TOTAL WEALTH VS. WEALTH EXCLUDING HOME EQUITY: BLACK HOUSEHOLDS

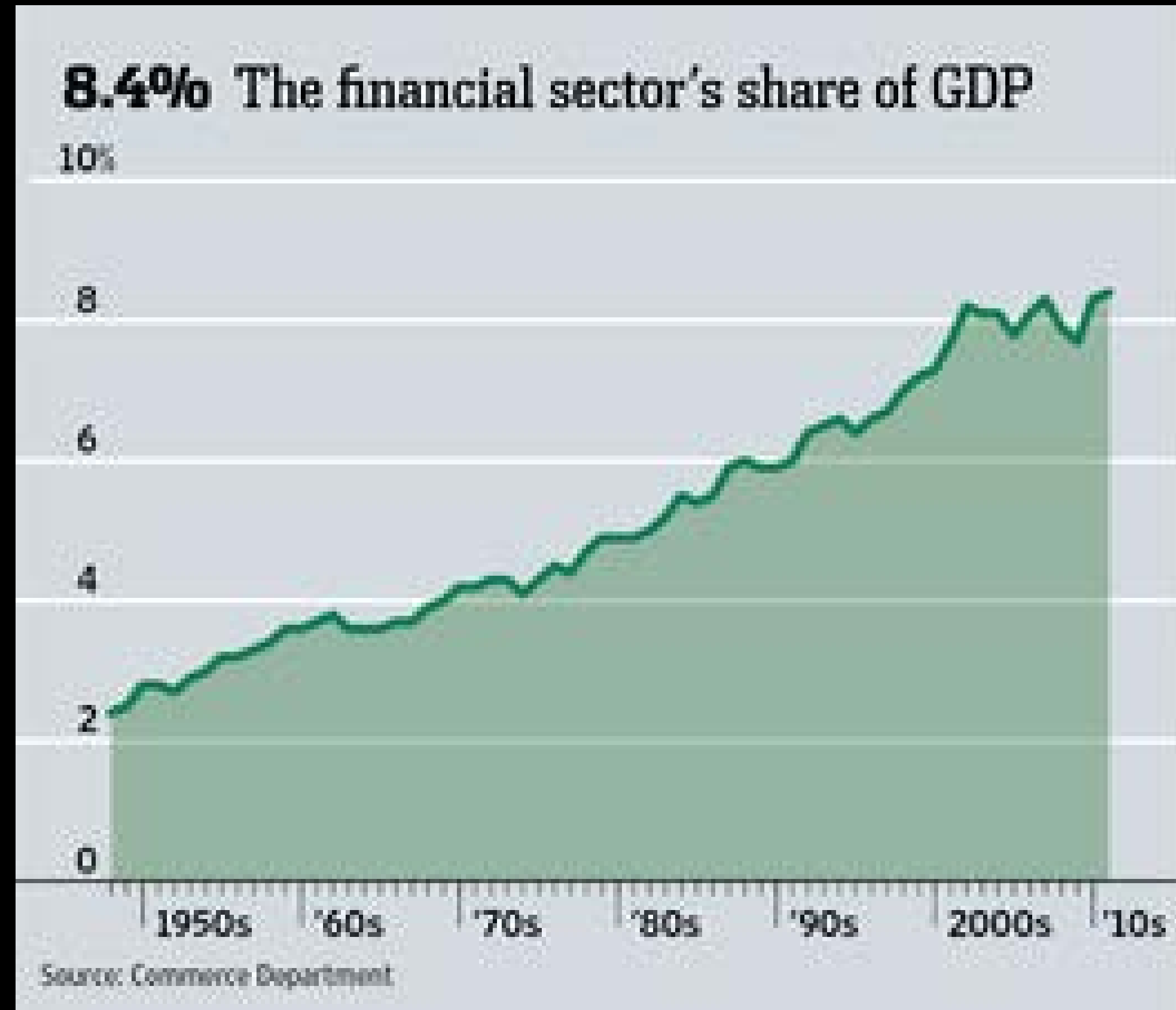
$70,000
$60,000
$50,000
$40,000
$30,000
$20,000
$10,000
$-

1999 2001 2003 2005 2007 2009 2011

Wealth Including Home Equity
Wealth Excluding Home Equity

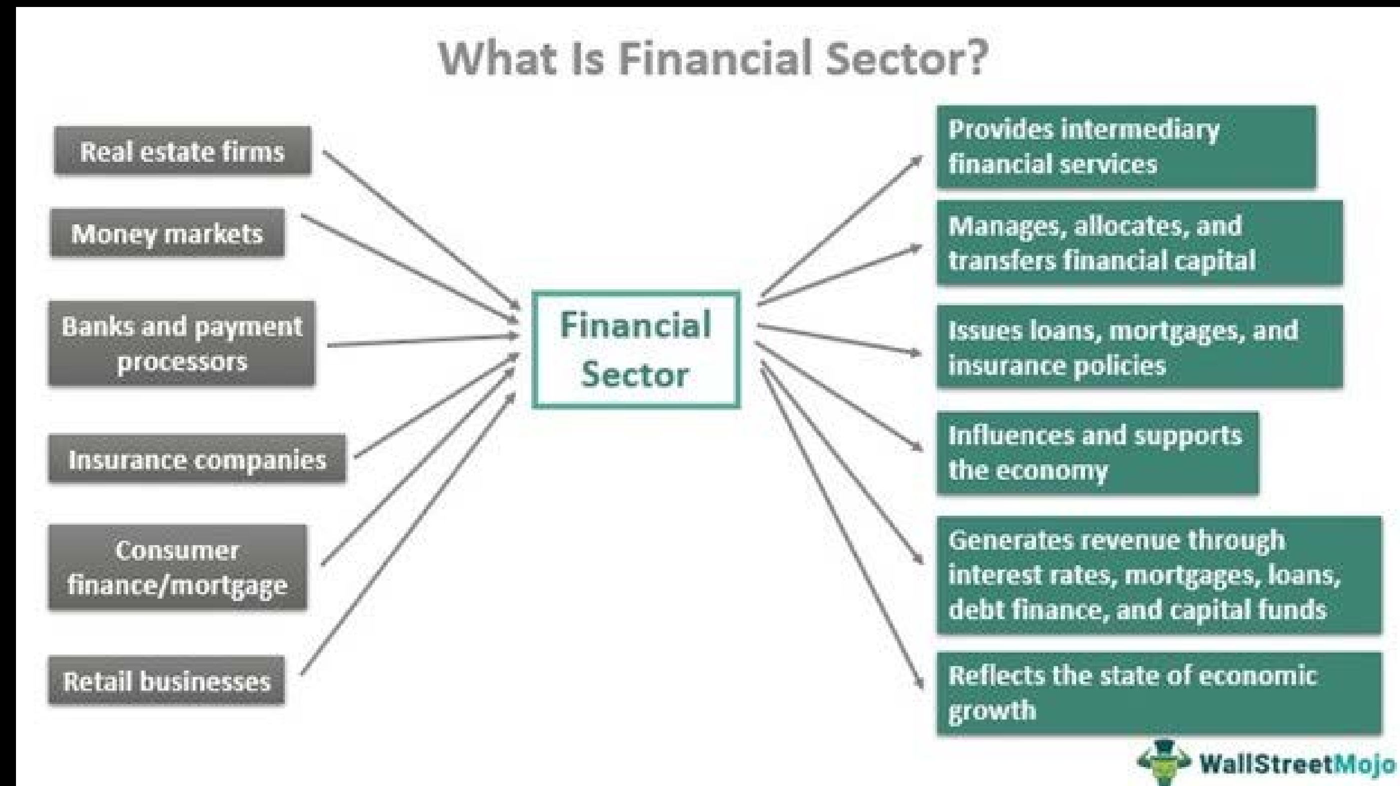
Financial Sector's Share of the Economy

- According to Hudson and Bezemer (2012): financial sector profits accounting for 40% of total U.S. domestic profits in the early 2000s—a steep increase from the 10% seen in 1950-60s.
- By 2011, finance and insurance made up 8.4% of the U.S. economy (i.e., Gross Domestic Product [GDP]).



What is the Financial Sector?

- According to the International Monetary Fund (IMF), the financial sector covers many different types of transactions in such areas as real estate, consumer finance, banking, and insurance. It also covers a broad spectrum of investment funding, including securities.



When fiscally strapped local governments reduce the risks and costs borne by private developers—through rezoning, tax subsidies (e.g., 421a), and divestment in public lands—those private housing developers can successfully leverage debt to enhance their portfolios by gentrifying neighborhoods while providing only a modicum of truly affordable housing. Renters are further squeezed when private equity firms buy their homes to grow their portfolios [Fields' reading this week].

Sources

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