Morgenson, Gretchen, and Joshua Rosner. *Reckless Endangerment: How Outsized Ambition, Greed, and Corruption Led to Economic Armageddon.* New York: Times Books, 2011.

1. Introduction

Reckless Endangerment is a noteworthy journalistic account of the causes of the U.S. credit crisis of 2008 and the deep recession that followed. The overall narrative follows the common understanding of the crisis's origins. The recession of 2008-2010 was precipitated by the bursting of a bubble in the U.S. real estate market. The bubble was driven by low interest rates and a booming mortgage market with high growth in adjustable-rate and no-money-down lending to financially risky borrowers (especially "sub-prime" borrowers). When the bubble burst, hundreds of billions of dollars in mortgages proved worthless, and the financial system in the U.S. and Europe nearly collapsed. *Reckless Endangerment* relates these events in a personalized, moralized fashion. It tells stories and names names, putting faces on the causes of the disaster.

The story begins in the 1990s, focusing on the CEO of Fannie Mae in those years, Jim Johnson. Fannie Mae and its sister institution Freddie Mac were nominally private entities set up by the federal government to promote homeownership by buying mortgages and selling mortgage-backed securities. The companies benefited from lax regulation and the ability to borrow money at lower rates than any other private company. Their borrowing power was due to the implicit guarantee that government would cover their debts (a guarantee that was proved to exist when the U.S. Treasury took them over in September, 2008).

Johnson made Fannie Mae into a political juggernaut and lucrative profit center, entering into a partnership with the Clinton Administration to promote increased homeownership through lowered lending standards. All of this was done in the name of expanded access to mortgages for the poor and for minorities. Fannie Mae built up a fake grassroots movement in favor of expanded mortgage access, and it could trot out examples of houses built and bought and protests organized any time its privileges came into question.

Achieving the goal of expanded homeownership beyond the already high levels of the early 1990s required making sure that people who hadn't received mortgages in the past could get them. The dogma of the time was that this merely required sensitivity and overcoming racism and other prejudices. But the truth of the matter was that most people who couldn't get mortgages couldn't get them because they couldn't raise the needed down payment or because they lacked the income needed to afford the mortgage

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payments. They were, in other words, bad risks. They weren't prime mortgage candidates; they were sub-prime.

So Johnson and his successor Franklin Raines led a concerted push to lower the evidentiary and income requirements for getting a loan: they called it "Alternative Qualifying." And the Clinton Administration chipped in with ever-rising requirements for the financing of "affordable housing." By the time Andrew Cuomo was Secretary of Housing and Urban Development (HUD) in the late 1990s, he was requiring that 50% of all mortgages be made to low-to-moderate-income borrowers.

The stage was set: lending standards were degraded and Fannie Mae and Freddie Mac led Wall Street into ever-expanded lending to the riskiest borrowers. It was in this context, after the dot-com bubble burst in 2000, that the Greenspan Fed drove the core interest rates down to 1% from their long-term range of 5-6%. With money practically being given away, and housing the only safe investment that was still rising in value, the U.S. was primed for an orgy of lending to anyone and everyone buying houses. From there, it was only a matter of time before the real estate bubble burst and overstretched borrowers began defaulting *en masse*.

2. Heroes and Villains

Reckless Endangerment is a journalistic history, not a scholarly one. It is written in lively, valorized language. What's at stake is emphasized in every chapter and on virtually every page. The basic structure of the book is to move chronologically from the early 1990s through 2008. Each chapter offers a story or stories focused mostly on particular businesses and politicians, with general remarks on overall trends for context. Citations are not provided. The brief notes on sources indicate that the book arose out of a trove of interviews that the two authors had collected while covering business affairs for a decade or more.

A typical chapter centers on shenanigans at Fannie Mae, sub-prime lenders, Washington, or Wall Street, made more dramatic by some episode of criticism that makes us think that, with better will or a more responsible culture, the crisis might have been averted. Unsung analysts are the heroes of the piece. As we move from the halls of the U.S. Congress to Georgia politics, to sub-prime lending in California and elsewhere, we are invited to sympathize with the struggles of what seem to be the authors' favorite sources. In evidentiary terms, the strongest sections of the book show through speech and action what the main figures were doing, and leave the reader to judge the meaning. The weakest sections in terms of evidence center on sympathetic figures (the sources) as witnesses, interpreters of events, and judges of character.

For instance, Chapter 9 focuses on an effort to impose severe restrictions on "predatory lending" in Georgia. The chapter's hero is William J. Brennan, Jr., a director of the Atlanta Legal Aid Society and an architect of Georgia's "fair lending law," which passed in 2002 and was defanged in 2003. Brennan attends a sub-prime lending conference, and we are told "It was clear to Brennan that the conference attendees were watching Georgia's attack on predatory lending with fear and loathing. . . . Brennan knew then and there that he and his colleagues had a fight on their hands" (p. 146). We are supposed to accept Brennan's interpretation, even though he is far from being a dispassionate observer.

From page to page, the book has an episodic, David-versus-Goliath narrative structure, but leaves many questions unanswered about the overall state of the market and the real causes of its problems. Similarly, because most chapters center on a nefarious central company, we get a tour through the most scandalous firms, ones that usually went bust later, including Novastar Financial and Countrywide Financial. But it is less clear what was typical of the industry or what the soundest companies were doing.

3. Complexity Over-Simplified

Another price of the episodic hero-villain drama and the valorized narrative is that the authors breeze over complex issues that deserve a fuller treatment. This is not a demand for a different book, but rather a wish that the book as conceived were more judicious.

For instance, the Georgia fair lending law was undone in 2003 by the refusal of the rating agencies Fitch and Standard & Poors to rate mortgage securities originating in Georgia (this in turn would ensure that the supply of mortgage financing in Georgia would collapse for both prime and sub-prime mortgages, since lenders typically re-sold their mortgages and needed agency ratings to do so). Over pages 147-51, Morgenson and Rosner paint this event as a nasty conspiracy of shifty lenders to keep the party going. But the law stirred such protest in the finance industry because it held buyers of a mortgage liable for acts committed by the original mortgage lender. This was not a liability any other market required, nor was it typical of any other commodity or stock. It is at least not obvious that such a strict collective liability rule ought to exist. Its nature and implications deserve more discussion than Morgenson and Rosner provide.

The book renders the actions and causes of the crisis into clear, plain language, as in all good journalism. But there are places where the broader context is summarized in an amazingly cavalier fashion. For example, on pp. 274-76, Morgenson and Rosner discuss the rise of interest-only loans and negative amortization loans (the latter are loans which have a payment schedule of under-payments whose shortfall is added to the balance due). Now, loans of both types are ill-advised except in exceptional circumstances. If the borrower must stretch to make payments on a loan of these kinds, he or she is unlikely ever to pay down the principal and retire the debt. That these two loan types rose from being 6% of loans in 2003 to 29% of mortgages by 2005 was a sure sign of the irresponsible lending and borrowing at the height of the bubble (when much of the borrowing public assumed that property values would simply rise and rise, lifting them out of their debt holes). That's the clear part.

But Morgenson and Rosner go on to write:

> By creating these loans, . . . Wall Street's bankers had done something entirely new and nefarious. They had allowed institutions extending credit to consumers in the form of a second mortgage or home equity line of credit to share in the collateral backing all the loans without asking for permission from lenders who were there first and thought they were the sole creditors. (p. 276)

Now this is very unclear, and from what I can tell, is basically false in its presumptions. Generally, the law holds that the first lien on a property by date has priority in a bankruptcy or foreclosure.[1] Generally, borrowers have never needed to get permission from other lien-holders before taking on new debt. It's just that most housing lenders won't lend without the security of being in first position on the lien. Furthermore, Wall Street is based in contracts: to upend the basic priority of lenders would require changing property law nationwide. That's not (yet) within the power of Goldman Sachs. What then are Morgenson and Rosner talking about? The reader shouldn't have to ask.

4. What Should Have Been Done?

Reckless Endangerment is a strongly normative book based on some clear counterfactual conclusions. For instance, if the Clinton Administration, Congress, and Johnson and Raines at Fannie Mae had not pushed throughout the 1990s to bowdlerize lending standards and incentivize lending to the riskiest borrowers, a sounder and saner mortgage market would have entered the new millennium. If Congress had fully privatized Fannie Mae and Freddie Mac, much harm could have been avoided, too.

More broadly, there is much anecdotal evidence here, including some data, that one could read comfortably from a libertarian, free-market perspective. Certainly, the book is a portrait of a politicized market gone wrong.

Nevertheless, the authors plainly mean instead to double-down on the premises of the welfare state. Chapter after chapter laments the toothlessness and fecklessness of the regulators. The (legally mandated) ratings agencies that declared dubious mortgage securities "AAA" are chastised for their blind, go-along-get-along attitude. Morgenson and Rosner imply that if only the regulators had wisely regulated, and Congress had wisely overseen, and the rating agencies had acted for the sake of the public trust, then everything would have been better. The trouble is, nothing in the book gives us much reason to think wisdom would arise in these quarters nor that these agents would have much reason to be wise.

The authors' idea of the poorly run company depends on a conception of the well-run company. But this is never directly described.

[1] See, e.g., http://www.nolo.com/legal-encyclopedia/what-happens-liens-second-mortgages-foreclosure.html.

Often, the well-run firm lurks in the background of the case studies in financial malfeasance. Fannie Mae in the 1980s is cited as well-run and responsible, before Johnson ran it off the rails. While Angelo Mozilo was the brash front-man of sub-prime titan Countrywide Financial, Morgenson and Rosner note that from 1968 to 2000 Mozilo had a partner in leading the firm, David Loeb (pp. 188-90). We are told that Loeb kept Mozilo's worst excesses under control and monitored risk levels carefully. Over this period, the firm grew and succeeded though many national financial ups and downs. That would seem to have represented a sound model for Countrywide. But what was that model? More could have been said.

Who actually has an interest in responsible lending? The authors seem to assume it is society or the taxpayers who ought to care, from the motive of altruism. But in truth, the people with the most at stake, directly and personally, day in and day out, would have been the shareholders and the borrowers.

Shareholders benefit from the long-term health of the companies they own: they are the ones wiped out first in a bankruptcy. They are the ones who most need reliable rating information from analysts and transparent accounting from the firm's management. But in *Reckless Endangerment*, shareholders are a passive set of victims. Perhaps they deserve decent earnings from their investments, but there is no lesson for them in the book's many exhortations. This is a pity, because if market capitalism is going to improve and learn better how to marry innovation to prudence, shareholders will have to demand improved management and better information.

Morgenson and Rosner likewise paint borrowers as the victims of predatory lenders. They trot out several anecdotes of hapless borrowers who were shafted by crummy deals and dishonest salesmanship. But to anyone who thinks of borrowers as moral agents, these anecdotes leave more questions than answers. One set piece (pp. 208-10) focuses on an Atlanta retiree named Patricia Jordan who, we are told, somehow went from a 9% adjustable-rate loan on a property that was worth $30,000 in 1983, to an adjustable-rate loan over 10% owing $124,000 in 2004. The authors focus on the deceptive marketing that Jordan recounts (she thought she was signing a fixed-rate mortgage when she took on the new debt). But huge questions pass by without comment: probably $100,000 or more of the new loan was unrelated to the original debt on Jordan's home. What was that money for? And Jordan was taking on a huge new debt, compared to her limited income. Why didn't she get some advice before signing the contract? These are the basic questions any borrower should be able to answer. The book doesn't give any evidence that Jordan asked them.

Predatory lending (which consists in selling high-priced loans to unsophisticated borrowers) is surely a problem, but any trade has two parties. The authors seem to forget than no one is forced to take on a loan, not even by high-pressure sales tactics. We need to hold borrowers and consumers more generally morally responsible for their actions. And books like *Reckless Endangerment* need to offer them clearer moral counsel. In our credit-driven society, where many borrow to spend without saving for the future, it is each of us as consumers who gains from having principles of prudence and long-range planning.

Reckless Endangerment is a lively read. It is a trove of anecdotes of malfeasance and mania. But despite its strong moral tone, it does a worse job than it could have in making clear what the better alternative would have been.

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