Faculty Forum, Rivendell Institute, December 11, 2008:  
**Moral Dimensions of Financial Crisis**  
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**What Happened? A Subprime Primer**
(http://www.som.yale.edu/faculty/Sunder/Subprime%20explainedOct2008SOMR.pps, the origins of this presentation are not known to me. If you happen to know the name of the author, please let me know for appropriate attribution).

**Probable Causes of the Financial Crisis**
1. Attempts by government to expand home ownership beyond those who qualified for traditional mortgages to those who may not have the resources for owning homes—the rise of subprime mortgages.

2. Residential homes increasingly came to be seen as commercial assets of value to be bought and sold as opposed to a permanent place of residence to be used and passed on the future generations.

3. Structure of mortgage markets: (Almost) everyone—the sellers, brokers, bankers, assessors, insurers, builders, and even buyers—benefited from rising home prices so there was little downward pressure on home prices to keep the in balance. This was combined with the widespread belief, encouraged by the real estate industry, that the home prices “always go up” encouraging entry of non-professional speculators into the real estate market.

4. Securitization of mortgages in increasingly complex instruments that were not understood by those who were persuaded to buy them.

5. Absence of incentives for due diligence on part of the mortgage initiators because they could sell the mortgages to others without recourse (switch from originate-hold-collect to originate-sell-no responsibility for collection mode for mortgages).

6. Conflict of interest on part of the derivatives ratings agencies (Standard & Poor’s, Moody’s and Fitch were paid by those who wanted them to rate the derivatives at high grades).

7. Ability of Fannie Mae and Freddie Mac to lobby Congress at massive scale to frustrate the attempts to properly regulate these giant public-private hybrid entities.

8. Failure of the Federal Reserve Bank and the U.S. Treasury to perform their regulatory duties in (1) preventing a real estate bubble through control of money supply, (2) preventing excessive leveraging in investment banking, (3) ensuring transparency of derivative transactions, possibly through a central registry and clearinghouse, and (4) formation of financial institutions which were “too big to fail.” Incidentally, since these
regulators continue to encourage, even facilitate, formation of even larger financial entities, this regulatory failure has become intensified instead of being mitigated since recognition of the financial crisis.

9. Willingness of the Securities and Exchange Commission and the accounting rule writers to allow large liabilities in the financial sector to remain hidden from view under opaque labels such as SIV (Structured Investment Vehicles).


11. Willingness of U.S. and EU to allow continuation of transactions with opaque financial regimes and tax havens (e.g., Switzerland, Caymen Islands, etc.)

Related Issues:
1. Provision of resources (food, shelter, education, healthcare, etc.) for those who have less, and need or ask for more. Who should decide and who should provide such support? Individuals or government or some other collectivity? How much?
2. Consequences of using public funds on demand for subsidies (charity with others’ money and its effect on systemic viability).
3. Consequences of subsidies for those who decide on them in a democratic polity.
4. Role of incentives/self-interest/greed in economic, social and religious systems
6. Alternatives to self-interest as organizing principle of society—altruism?
7. Efficiency and inefficiency of scale (e.g., in the banking system).
8. Balance between decentralization (freedom of individuals and groups to act) and monitoring (control to make sure that these actions do not bring harm).
9. Cartesian (top down design from omniscient knowledge) and Darwinian (bottom up emergence through complex and hard-to-understand interactions among elements of the system) approaches to development of social systems.
10. Consequences of keeping the (car?) factories open with public money.
11. Contracts: financial, economic, social, metaphysical (Russian dolls structure?)