



# How Globalization Impacts Housing Finance

The proverbial adage about one’s inability to see the forest for the trees seems more applicable than ever in today’s mortgage industry; professionals throughout the lending vertical are focused on the state of U.S. housing, while a bigger economic issue looms—the globalization of our mortgage and real estate financing. **By Toni Moss**

In the early 1970s, a paleontologist in eastern Nebraska discovered the fossilized remains of 200 prehistoric animals killed by a volcanic explosion 10 million years earlier. Around the same time, a parallel discovery was made a thousand miles away in Idaho. The remarkable similarities of the two sites instigated scientists’

search for a “super volcano” large enough to cover half of North America with two meters of ash. Their search led to Yellowstone National Park. However, they couldn’t find a crater large enough within the park to cause an explosion of that magnitude. After years of searching, one of the geologists approached NASA for infrared images of the area

from space. The images revealed that the crater of the volcano they were looking for was a caldera 45 miles across and 35 miles wide, encompassing nearly all of Yellowstone Park. Even the most experienced of geologists could not find the crater of the super volcano because they were right in the middle of it. It was all around them.

This story illustrates the importance of changing our perspective to see the bigger picture. In the world of housing finance, we face a situation similar to the one that puzzled the geologists. Since the implosion of the U.S. housing finance industry in 2007, investigations and analyses have continued to reveal the need for major changes in the processes and practices of our industry. However, these findings have done little to change the notoriously myopic perspective of the housing finance industry. Considering the fact that a mortgage is the greatest amount of money that most people will ever borrow in their lives for the longest period of time; that mortgages have been the anchor product for almost all financial institutions; that housing makes up a large percentage of the GDP of almost all nations of the world; and that real estate and mortgage-backed securities comprised the single largest asset



class in global capital markets, by 2005 it was clear to see that housing finance had become the epicenter of the global economic fault line.

Yet most industry leaders around the world were uninterested in looking beyond their own national markets to see that bigger picture or their role in it. Part of this is due to the fundamentally local nature of housing. However, when Ginnie Mae issued the first mortgage-backed security in 1970, the funding of local housing became global. From that moment on,

we benefited from an increase in the volume and flexibility of U.S. mortgage products as well as lower interest rates directly due to this exponential rise in foreign funding. The benefits to the U.S., however, were ultimately one-sided. As such, the liquidity of foreign funding will continue to diminish until we resolve the high-profile problems and litigation currently under way and, more important, get clarity from our current administration on the direction in which their efforts will steer the market in the future.

To date, we all know that despite best efforts, government intervention intended to stabilize the market has fallen short of its goals and continues to prevent knowing exactly where the bottom of the market actually is. Finally, the nations from which funding for the U.S. mortgage market came now face their own economic woes. What happens to the U.S. market if the spigot is turned off, and how many firms incorporate that scenario into their strategy?

Now that the economic fault line has ruptured globally, we are left with an industry in

desperate need of direction and reconstruction. However, I would argue that we will not find direction or solutions until we as an industry see the bigger picture. The bigger picture is globalization. It is the issue of our lifetime.

### What Is Globalization?

“Globalization,” like the caldera of the super volcano, is all around us. It is often confused with internationalization,

## CONNECTEDNESS AND CONVERGENCE

**“We have embodied our rationality within our machines and delegated to them many of our choices, and in this process we have created a world that is beyond our own understanding. Our century began on a note of uncertainty, as we worried how our machines would handle the transition to the new millennium. Now we are attending to a financial crisis caused by the banking system miscomputing risks . . .**

**“We have linked our destinies, not only among ourselves across the globe, but with our technology. If the theme of the Enlightenment was independence, our own theme is interdependence. We are now all connected, humans and machines. Welcome to the dawn of the Entanglement.”**

- Danny Hillis (2010 - www.edge.org)

The concept of “housing finance” illustrates both the reach and the dilemma of our industry in a globalized world. The lifecycle of our activities and the quality and performance of our products and services have a very distinct and direct socioeconomic and political cause and effect at local, regional, national, and global levels. The direct cause and effect is intensely personal as well. From the freedom and achievement of homeownership to the devastation of foreclosure, and from the pension of a German schoolteacher to the livelihood of American taxpayers, we can never forget that our professional actions and decisions in this industry have deeply personal consequences all over the world.

The interconnectedness that characterizes globalization demands cooperation and compromise, and an understanding that even the best actions will cause unintended consequences in an interconnected world. This is precisely why this prolonged crisis continues relatively unabated. By far, the greatest change today is the velocity of change. Not only is the world under (re)construction, but also the tools and strategies of the past no longer apply to the challenges of today. By the time we implement an intended solution, the playing

field has changed and a new problem has emerged. This is the impact of globalization. Therefore, from this point forward, we’re left with making it up as we go along. As we all vary in degrees of optimism and despair over what the future holds, the trial and error process of invention is helpful to keep in mind. At the risk of simplicity, we need to strategize, not criticize.

In the quote above, scientist Danny Hillis elegantly describes the contrast between the independence of the Enlightenment and the interdependence of what he calls the “Entanglement.” The most striking aspect of Hillis’ observation says much about the actual force of globalization: Whereas the independence of the Enlightenment was driven by the will of individuals, the interdependence of the Entanglement—or what I call “convergence”—is not driven by conscious choice but by the forces of globalization.

Because our activities in housing finance are part of a lifecycle as opposed to a value chain, we each play an equally important role in ensuring its fluidity and continuity. Therefore, regardless of our roles in the industry, we must all fundamentally understand the basics of the entire mortgage lifecycle. More important, the basic curriculum of industry education should

incorporate a multidisciplinary approach to globalization. That approach means incorporating disciplines such as philosophy, ethics, political science, history, public administration, demographics, urban planning, et al., and not just business and economics. While no one wants to be told what to think, everyone benefits from learning more about how to think and broadening their horizons.

In taking responsibility for our own role in the crisis, I believe the housing finance industry has an obligation to offer solutions, with the caveat that those solutions will only come from a change in perspective that contemplates the realities of a globalized world. I opened the EuroCatalyst 2002 event in Madrid with the statement, “As a global industry, we need to lead in our solutions for a globalized world and not become victims of it.” We still have that chance.

Globalization offers as many opportunities as detriments. The more we know about it, the more able we are to seize the opportunities and create contingencies for the detriments. In the housing finance industry, we need a higher caliber of leadership, education, and dialogue to discuss and debate the complexities of these issues. Using the example of the geologist who sought outside advice from NASA to solve his dilemma, we need to “cross-pollinate” our own knowledge and expertise with experts from outside of the industry to create more collaborative solutions and external perspectives. However, we cannot and should not outsource our thinking to others. If we cannot see the world and the interactions shaping it, we cannot prepare for it, nor can we create strategies or solutions for it. Once you do see it, you will never see it in the same way again.

which refers to relationships among nations engaged in international (as opposed to global) trade, relations, treaties, alliances, etc. However, globalization is something entirely different. To define it would inevitably exclude some important aspect of it; therefore, it is more frequently described than defined.

At a very basic level, “globalization” refers to the global economic integration of formerly national economies into a single global economy through free trade and capital mobility. On a more complex level, globalization is the convergence, integration, and interaction of a wide range of social, economic, political, technological, biological, and cultural trends in a process that transcends local, national, and regional boundaries. It affects everything around us, from the way we think and communicate, to the ways in which we are governed, to the products we buy and sell, the foods we eat, the energy we use, and the wars we fight.

Unlike in the past, the debate is no longer about whether globalization exists or whether we have a choice in its evolution. Today’s debate surrounds the type of framework needed for the world to more fluidly accommodate this ongoing and irreversible process that fundamentally alters our social existence with profound implications for virtually every facet of our lives.

In the housing finance industry, most of us are familiar with the economic aspect of globalization that enables free markets and cross-border capital flows, international trade and labor—including outsourcing—and global risk transfer facilitated by securitization. But the globalization process changes our perceptions of space and time, delocalizing issues, magnifying risk, accelerating change, forcing transparency, and transforming our most basic institutions from culture and traditions, to family structures, to theory and ideology and the nation-state. Thus globalization impacts every single aspect

of the housing finance industry, from basic supply and demand, to the mortgage products we create, the information and services we provide, the way in which (and whether or not) our mortgages are funded, and even the types of homes we build. The strategy and survival of every company operating at every stage of the housing lifecycle is affected, some in more specific ways than others.



## Government and Regulations Go Global

One of the most noticeable characteristics of globalization is the blurring of sovereign boundaries and the role of the nation-state. In a global marketplace, the globalization process erodes national powers, forcing nations to constantly redefine and reinvent themselves. Sometimes the reinvention process is beneficial, such as the recent uprisings and democratization efforts in the Middle East. Other times, the process is excruciatingly painful, as we’ve witnessed in recent fiscal debt discussions. What we will see more frequently in the future

is the inability for certain nations to adhere to certain ideologies and values in the face of global financial concerns. At a very basic level, we see this process of redefinition and reinvention occurring in debates over the role of the federal government in housing finance and housing policy with regard to the GSEs.

Keeping in mind that the failure of U.S. subprime securi-

markets were not contemplated when existing regulatory bodies were first formed, we should also expect more shifting of the roles and responsibilities among regulators, not less of it.

## More Than the End of an Era?

A few writers, in particular Francis Fukuyama and Kenichi Ohno, suggest that the most significant aspect of today’s intensified stage of globalization is a break with the past. Fukuyama goes so far as to call it “the end of history,” although he later acknowledged the incompleteness of his thesis. Incomplete or not, it is a compelling concept. Perhaps we have reached the end of history in the sense that the problems we face today are so dramatically different from those of the past that every attempt to solve them is nothing more than a grand social experiment, the outcome of which remains unpredictable and unknown.

As this crisis has shown, we appear to have outgrown our institutions—and quite possibly have reached a world of intellectual endings. After all, the world today looks entirely unlike the world envisioned by the Enlightenment philosophers of the 17th century, who conceived our fundamental notions of freedom, democracy, reason, egalitarianism, and established the market mechanism for capitalism, among others. The Enlightenment was characterized by rational, critical, and open discussion of public issues once dominated by state and religious authorities. Considering the increasing political polarities, intellectual dogma, and moral hazards posed by this crisis, perhaps it’s time for a new Enlightenment, in which we re-evaluate and reinvent traditions to fit the challenges and reality of the 21st century. Of those traditions, surely one of the most important to consider is how we live, where we live, and how we pay for it.