

Nationalization of Fannie and Freddie: Most radical regime change in global economic and financial affairs in decades

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The now inevitable nationalization of Fannie and Freddie is the most radical regime change in global economic and financial affairs in decades. For the last twenty years after the collapse of the USSR, the fall of the Iron Curtain and the economic reforms in China and other emerging market economies, the world economy has moved away from state ownership of the economy and towards privatization of previously state owned enterprises. This trend was aggressively supported by the United States that preached right and left the benefits of free markets and free private enterprise.

Today instead, the US has performed by far the largest nationalization in its history. By nationalizing Fannie and Freddie the US has increased its public assets by almost \$6 trillion and has increased its public debt/liabilities by another \$6 trillion. The US has also turned itself into the largest government-owned hedge fund in the world: by injecting a likely \$200 billion of capital into Fannie and Freddie and taking on almost \$6 trillion of liabilities of such GSEs the US has also undertaken the biggest and most leveraged LBO (“leveraged buy-out”) in human history that has a debt to equity ratio of 30 (\$6,000 billion of debt against \$200 billion of equity).

“Socialism” is indeed alive and well in America; but this is socialism for the rich, the well connected and Wall Street. A socialism where profits are privatized and losses are socialized with the US tax-payer being charged the bill of \$300 billion.

This biggest bailout and nationalization in human history comes from the most fanatically and ideologically zealous free-market laissez-faire administration in US history. These are the folks who for years spewed the rhetoric of free markets and cutting down government intervention in economic affairs. But they were so fanatically ideological about free markets that they did not realize that financial and other markets without proper rules, supervision and regulation are like a jungle where greed – untempered by fear of loss or of punishment – leads to credit bubbles and asset bubbles and manias and eventual bust and panics.

The ideologue “regulators” who literally held a chain saw at a public event to smash “unnecessary regulations” are now communists nationalizing private firms and socializing their losses: the bailout of the Bear Stearns creditors, the bailout of Fannie and Freddie, the use of the Fed balance sheet (hundreds of billions of safe US Treasuries swapped for junk toxic illiquid private securities), the use of the other GSEs (the Federal Home Loan Bank system) to provide hundreds of billions of dollars of “liquidity” to distressed, illiquid and insolvent mortgage lenders, the use of the SEC to manipulate the stock market (restrictions

on short sales), the use of the US Treasury to manipulate the mortgage market (Treasury will now for the first time outright buy agency MBS to manipulate and prop up this market), the creation of a whole host of new bailout facilities (TAF, TSLF, PDCF) to prop and rescue banks and, for the first time since the Great Depression, to bail out non-bank financial institutions, and a whole range of other executive and legislative actions (including the recent bill to provide a public guarantee to mortgage for banks willing to reduce their face value).

This is the largest State intervention in a capitalist economy. So foreign investors can earn fat spreads relative to Treasuries on agency debt and never face any credit risks (not even the subordinated debt holders who made a fortune yesterday as those claims were also made whole).

Like scores of evangelists and hypocrites and moralists who spew and praise family values and pretend to be holier than thou and are then regularly caught cheating or cross dressing or found to be perverts these Bush hypocrites who spewed for years the glory of unfettered wild west laissez faire jungle capitalism (and never believed in any sensible and appropriate regulation and supervision of financial markets) allowed the biggest debt bubble ever to fester without any control, have caused the biggest financial crisis since the Great Depression and are now forced to perform the biggest government intervention and nationalizations in the recent history of humanity, all for the benefit of the rich and the well connected.

These laissez faire zealots in charge of the US economy have now caused the biggest financial crisis since the Great Depression and the nastiest economic crisis in decades. So let them be shamed in public for their hypocrisy and zealotry that has caused so much financial and economic damage.

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