CLUELESS SUITS

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Your faithful reporter can state with no exaggeration that he has spent days -- nearly every waking hour (no kidding) -- deep in study, in a crazy-making attempt to achieve at least a kindergarten understanding of our present financial crisis. And he promises you that if you, too, spent days perusing jargon-jangled articles packed with sentences in which clauses and sub-clauses abut one another in a maze of anti-clarity, subverting both grammar and sanity, then you, too, might refer to yourself in the third person, if only to achieve some illusionary distance from the blazing eyes of the stark-staring madness that roils beneath the tidy title "economics."

Pity anyone who attempts to absorb the meanings of such usages as 25-standard deviation moves (which is actually one thing, sort of, not 25), commercial paper (it's not what you might think), exposure, neo-credit, securitization, private-label issuers, asset-backed securities (also not what you might think), jumbo-mortgage providers, multi-strategy funds, quantitative funds (quaintly called "quants"), subprime, collateralized-debt obligations, off-balance-sheet units, and how an "Internet bank" is very different from a "brick-and-mortar bank." Since the newspaper and broadcast talking-heads who comment on the crisis mostly employ this jargon, TV news barely covers it (except for CNBC), and the print accounts are mostly bores. Most citizens not in direct danger of losing their homes are aware only that the housing market is slumping, the stock markets are behaving wildly, the Federal Reserve Board has responded someway or other, and things may or may not have calmed down a little, and what has that to do with us?

Yet the crisis is real, probably systemic, and may be dire (that is, eventually it may hit us). In general terms and plain English, it can be explained in a paragraph. In recent years numerous mortgages were granted, knowingly and unknowingly, to folks who couldn't afford them; the banks also sold many mortgages to folks who could afford them. The banks bunched all these mortgages, both the sound and unsound, into packages, then sold those packages to investment companies. These investment companies packaged many mortgages-packages together and sold them to bigger investment companies -- *really* big investment companies, involved in *really* big deals. Those *really* big investment companies used these mortgage-packages as collateral for their really big deals. When shaky ("subprime") mortgages started defaulting, it meant that those mortgage-packages weren't worth as much as everyone had believed; therefore, the *really* big investment companies don't have as much money and credit as they thought they did -- and that, in turn, scares the crap out of lenders up and down the line, who've suddenly become reluctant to loan money to anybody, even individuals and companies with proven credit. In short: A humble level of the economy has weakened the elite; hardworking folks losing their dream-homes have subverted -- through machinations of which they're totally unaware -- the dealings of stratospheric executives. How may this hit you and me? When business is afraid to do business, things freeze up. If that goes on long enough, it creates a recession. In a recession, everybody hurts, especially the working and working-middle classes.

Once you get that general picture, the particulars aren't important for us economic civilians. There's no way we can control it and things will fall out as they fall out.

But there's an aspect to this situation that's fascinatingly absurd (if not actually funny). All those highly paid suits whose job it is to know what's going on -- they didn't have a clue. Cluelessness runs through this story like an underground river of lava that finally has erupted into what may become an economic volcano.

The front-page headline in *The Wall Street Journal,* Feb. 22: "Central Banks Confident in Stable Growth." In April, our own treasury secretary, Henry Paulson, "declared that all the signs he saw indicted that the housing market was 'at or near bottom'" (*The New York Times,* Aug. 17, p.23). In May, Ben S. Bernanke, chairman of the Federal Reserve, said, "We do not expect significant spillovers from the subprime market to the rest of the economy or to the financial system" (*The New York Times,* Aug. 19, p.1). Wrong. That's exactly what has happened. The media-sainted Alan Greenspan also got into the act. "Bankers… were not the only ones who encouraged borrowers to take out adjustable rate mortgages at precisely the wrong time. So did Alan Greenspan, the longtime chairman of the Federal Reserve" (*The New York Times*, July 27, p.C4). Even haloed Alan was clueless.

Stable growth? Housing market at or near bottom in April? "More borrowers with good credit [are] falling behind on their loans and the housing market might not begin recovering until 2009 because of a decline in house prices that goes beyond anything experienced in decades" (*The New York Times,* July 25, p.1). "[A]ssurances that the economy will be fine, such as the one delivered on Friday by Treasury Secretary Henry Paulson Jr., ring hollow in the absence of an international reporting framework to monitor the positions taken by globally active hedge funds" (*The New York Times,* July 30, p.16).

Got that? There's no system in place by which governments can even guess what the biggest money-players are doing, so how can our policy-makers possibly make policy?

"'It is impossible at this stage to judge how large and how persistent this tightening of credit conditions is likely to be,' [said] Mervyn King, the governor of the Bank of England" (*The New York Ttimes,* Aug. 10, p.1). Top British money-guy, clueless. Same article: "Many experts say the nation's mortgage problems are likely to worsen… as *hundreds of billions in adjustable-rate loans* [my italics] reset to higher rates in the next 12 to 18 months. At the end of March, nearly one in five subprime homeloans were either past due or in foreclosure." Nevertheless, that article quoted President (clueless) Bush: "The fundamentals of our economy are strong."

"Using what are known as market-neutral strategies designed by computer models, hedge fund traders have been blindsided by a correlation between bonds and stocks that they never expected would occur… Analysts call it model misbehavior" (*The New York Times,* Aug. 12, p.BU1). Is that wonderful or what? The suits aren't misbehaving; the models they use are misbehaving. "The people at Goldman Sachs lost a packet [that's a lot of money] when something happened that their computers told them should occur only once every 100 millennia" (*The Economist*, Aug. 18, p.9).

Said Liz Ann Sonders, chief investment strategist at Charles Schwab, "None of us are going to be able to time our moves" (*The New York Tmes,* Aug. 13, p.1). The models have gone awry because they were programmed cluelessly, and the chief investment strategist at one of our biggest financial firms admits cluelessness.

Two days before the markets went really haywire, "the [European Central Bank]… declared that recent financial turmoil was largely over… [its president said] in an unusual statement that 'market conditions have gone progressively back to normal.'… [Added the president of the German Bundedbank], 'We have confirmed our impression that the increased risks in certain market segments are insulated and that the profit impact for credit institutions is limited over all'" (*The New York Times,* Aug. 15, C3). Clueless.

You don't have to know how "commercial paper" functions; it's enough for our purposes to know that commercial paper is at the heart of this mess and that "until recently, the $2.2 trillion commercial paper market was considered one of the safest on Wall Street" (*The New York Times*, Aug. 18, p.C1). For our purposes, you don't have to know that SIVs means "structured investment vehicles," and you don't have to know what they do, but they've gone silly, too; yet "as late as June, Moody's issued a report calling SIVs 'an oasis of calm in the subprime maelstrom'" (*The Economist*, Aug. 18, p.63). That article also notes that the financial instruments involved are so baroque that, at the highest levels, "none of the players really knows how much he has lost." (What?!)

"Just 10 days after declaring the economy didn't need its help, the Fed declared 'downside risks to growth have increased appreciably' (*The Wall Street Journal,* Aug. 20, p.8). After the most haywire day in this crisis thus far, Clifford Asness, co-founder of AQR Capital Management, said, "In theory, what just happened is impossible" (*The New York Times,* Aug. 18, p.C1). Cluelessness reigns.

The Economist, Aug. 18, p.9: "Anyone who says the worst is definitely over is either a fool or someone with a position to protect." No one knows. High and low, no one is in control. As Lenny Bruce once put it so well, "Everybody's ass is up for grabs."

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