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Beyond the Rate – Chapter 15

Is anyone telling the TRUTH in the mortgage business??

Hello and welcome to Beyond the Rate, a series of podcasts that are designed to educate the listener on the world of finance and in particular, the mortgage business. This is Chapter 15, my last planned chapter. We'll be taking a broad brush look at capitalism and democracy. The changes I expect in the coming years will put pressure on our version of democracy here in America and I suspect capitalism will win in the end.

My name is Patrick and I'm a Mortgage Banker here in the San Francisco Bay Area. I'm your host and I really encourage you to subscribe to this series for an informative and detailed account of how the mortgage industry operates and how to navigate through all the confusing programs and deceptive marketing techniques being used by some of today's Mortgage Brokers.

Please note that the text versions of these podcasts are now available (in PDF format) for free download at my website at www.beyondtherate.com along with a bunch of other related materials and resources. You can also sign up for my monthly email newsletter at that website.

You may be wondering how I managed to get all the way to these nebulous broad-brush topics from being a Mortgage Banker. It's true. They seem distantly related at best. But there ARE connections between all these different topics and I think it's important to take a closer look where possible. Perhaps, we'll find some insights that benefit our future business decisions, and that's my goal in discussing it.

Most people believe that democracy is THE central pillar of American culture but I disagree. It may be in second place but I would reserve top honors for capitalism. Capitalism is the slightly less-appealing term for what we generally refer to as free-market economies. Same thing but free-market economies tends to sound a bit better so our elected politicians consistently use those words. We're free! We believe in freedom! And so on. Here in America, our freedoms are pinned up on every billboard. But at the end of the day, it's the freedoms of our BUSINESSES that truly define our society.

Back in university, my political science professor told us the best way to understand American foreign policy is to replace the word “democracy” and the word “freedom” with the word “capitalism” in all political statements and public speeches. Not bad advice, then or now. Fact is; it’s capitalism that makes all these freedoms and our democracy possible. If capitalism didn’t exist, you can bet many of our other freedoms would disappear right along with it. And democracy would be a lot harder to maintain if our markets required mandatory pricing structures or predetermined business partnerships.

Capitalist (or “free-market”) economies function on the premise that natural market forces determine prices and competition results in the survival of the fittest, leaving us all with the best possible products at the lowest possible prices. If demand for a particular product rises, the price rises as well. Think about today’s oil prices. And if demand for a product declines, the price falls as desperate sellers try to keep people buying. Think about the American car industry. It makes sense.

Obviously there are other economic systems out there; socialism and communism and so on. But the truth is that capitalism delivers the goods. Every time. Looking back through history, capitalism has always outperformed other systems by catering to human ingenuity and, frankly, human greed. Capitalism has some downsides for sure – like the persistent division between rich and poor – but it provides more overall prosperity than any other system. And it requires the least amount of bureaucracy at the same time.

The point I’m driving at is that democracy – the freedom to elect your own government – is a convenient byproduct of capitalism. If natural market forces regulate all product and service transactions, the role of government is primarily to protect that system. If the government is successful in creating an environment conducive to capitalism, the economy prospers and the population enjoys low unemployment and tax revenues allow for a variety of public services like schools, libraries, social security, police and the military. If the government does things to restrain capitalism, the system breaks down, unemployment rises and the population votes their government out of office through the democratic process.

There’s no need for a dictatorship because the underlying economic system is not in question. Everybody agrees that a free-market economy should be maintained and no political party in THIS country would dare challenge that notion. As long as the economy is healthy and people have jobs, the party in power usually enjoys stable support among the electorate. Problems arise when the economy weakens and people start losing jobs. That’s when people feel disenfranchised and start looking for better alternatives. That’s when approval ratings drop and the party in power often gets voted out.

As you know from listening to past chapters, I believe we are just finishing the largest financial boom we’ll see for many many years. I believe it started in 1982 and is slowly coming to an end over the next few years. So what can we expect going forward? If we’re approaching an era where recessions are more common and boom years are harder to come by, what will happen to our political process?

Well, probably nothing. I mean, I'm not expecting some crazy revolution simply because times are a little tougher. But I AM expecting an adjustment period where the general public gets educated on the new economic realities and the reasons behind them. The experts and pundits will eventually come out of the shadows and explain the change in fortunes and people will settle into a different set of expectations. But before that transition takes place, I would expect a much more turbulent political environment, probably starting in 2010 or 2012.

Democracy requires economic prosperity for survival. In fact, more than anything else, democracy requires a healthy job market. And a healthy job market doesn't require economic stability; it requires economic GROWTH. Our population is growing so the economy needs to grow each year just to keep pace with the population. If the population grows by 3%, the economy has to grow by 3% as well, just to maintain the status quo. If the economy goes sideways or enters a period of recession, the unemployment figures suffer immediately. And unemployment is the biggest enemy of established power.

You can see this everywhere. Population segments with high unemployment always have more problems than those with low unemployment. This is one of our government's primary goals in Iraq – get people employed. Hire them as police. Hire them for reconstruction projects. Whatever. Just get them working because lower unemployment will immediately reduce the violence on the streets. People need to feel like the system they're a part of benefits their own lives, and a good job does that.

The terrorist motivation comes from this same reality. Unemployment. We're talking about people who literally live on TOP of the biggest oil fields in the world. They see the glistening towers in their urban centers. They see the massive oil tankers leave their shores. They see the oil pipelines crossing their borders. They see the money and opulence corrupting their governments. They see all this wealth right in front of their eyes, everyday – but they can't even touch it. They're unemployed, bored and angry. Is it any surprise they direct their anger at the western nations who pay \$70 a barrel for the liquid being pumped from beneath their feet, much of that money going to their governments and almost none of it going to them? Is it any surprise they see capitalism as the root of all evil in the world? Is it any surprise the Saudi royal family is despised by most of their domestic population and indeed, by most of the region? Of course not.

Saudi Arabian citizens pay absolutely no taxes. They receive free education and free medical insurance, yet they've been bordering civil war for years. Yes, the royal family has managed to keep things remarkably calm but the resentment has been growing for years. Why? Because people want to be productive. People want to work. People want to contribute. And people want to benefit from the system they're a part of. They can be sedated with lavish services and interest-free loans for a while, but the fix eventually wears off and the anger sets back in.

The holders of power have always understood that high employment secures their power. And they have also understood that persistent UNemployment requires a strong police and military presence if their power is to be maintained. This explains the brutality in many struggling nations around the world. It also explains the focus on police enforcement in many struggling neighborhoods right here in America.

Interestingly, war is another reality that tends to encourage social stability and maintain existing power structures. It's very interesting to hear the political banter these days surrounding our efforts in the "war against terror". The issue has evolved into one of patriotism. Any decent of those efforts are labeled as unpatriotic. Am I suggesting it's all just a farce? No. Am I suggesting some sort of conspiracy in this regard? Absolutely not. But it's still fascinating to see how effective the effort has been in subduing political decent among Americans. There's no question that George Bush benefits politically from the war so long as progress, however modest, is made.

Anyway, if we enter an era of challenging economic times, I believe we'll see a steady increase in police enforcement that will be accompanied by an increasing division between the employed who blame crime for the economic hardship around them and the unemployed who are forced to live with boredom, hopelessness and anger. In the end, the true problem is that the boom years have simply subsided for a while and those who are negatively affected by the slowdown will be left bored, frustrated and looking for better alternatives to improve their lives. In many cases, that leads to violence.

Increasing violence here at home will fuel the conservative movement as people feel resentment towards the perpetrators of violence. Of course, the violence will come from those population segments where unemployment is the highest and those segments will exist within minority and undereducated circles. Resentment can easily morph into hatred and racism unless the underprivileged group finds a voice to properly explain the nature of their plight. This happened in the 60s when Martin Luther King Jr. brought an inspirational human voice to the anger in black America.

You can see this situation in many European countries. Unemployment rates are much higher there than they are here and local populations are increasingly resentful of immigrants coming from the eastern European countries. Violence has been on the rise in many of these countries and the underlying problem has little to do with the messages and slogans that make the evening news. The underlying problem is unemployment and a challenging economic environment.

So what will we see here in America in the years to come? Who knows? Will we see more challenging economic times? Probably. Will that lead to higher unemployment? Probably. But will it be severe enough to cause these types of chain reactions? Maybe not. It all depends on the solutions we find for the changes coming our way. I believe we are now in a period of slowly rising interest rates. I also believe we are in a period of slowly rising oil prices. And thirdly, I

believe we will see the value of the American dollar drop in the coming years, fueling inflation.

All of these things will dampen economic performance unless new innovations are developed to curb the tide in our favor. I have said all along that human ingenuity produces remarkable innovations and America has always been a beacon for human ingenuity. But the resounding priority will be employment and economic weakness will be met with increasing DE-regulation. Here in America, capitalism will always win, even if it widens the gap between the rich and the poor.

It's this gap between rich and the unemployed that results in the resentments to begin with, whether it's here in America, the suburbs of Paris or the oil fields in Saudi Arabia. This uneven distribution of wealth is the primary negative byproduct of a free-market economy. And to varying degrees, all "developed economies" are built on free-market economies so they all deal with these resentments one way or another. The taxation system is the primary tool governments use to balance these competing extremes. Taxes are collected from everybody but generally pay for services benefiting only the low or middle classes, effectively diverting wealth from the rich to the poor.

When politicians talk about deregulation or reducing taxes, they're talking about minimizing business oversight and social programs. The less wealth that is redirected from the rich to the poor, they argue, the more the economy can grow and flourish. George Bush is clearly a proponent of this view. But these efforts widen the gap between rich and poor, fueling social unrest. If the efforts are allowed to continue, the only remaining service would eventually be police enforcement. And when the police system fails, you slide into revolution.

Politically, this process describes the far 'right' position. The ultimate free-market economy. True capitalism. Here in this country, the 'left' position still embraces a free-market economy but it advocates business oversight and social programs to minimize corruption and balance the uneven distribution of wealth. Less tax, more tax. Less regulation, more regulation. Less government, more government. This IS the debate, after all. But if tough times ever led to a showdown between democracy and capitalism in America, I believe capitalism would always win in the end.

I'd like to thank you for listening to this podcast. This series began back in January and it's now almost June. This is my 15th chapter and we've covered a lot of detailed information in the mortgage industry and some broad brush concepts affecting the greater economy. I sincerely hope you've enjoyed them as much as I have. If you haven't listened to all 15 chapters already, I hope you do in the days and weeks to come. There's a lot of good information in there and knowing more will never hurt you.

If you're considering a purchase or a refinance, please call me to discuss the options. I'm a Mortgage Banker. It's what I do for a living. Interest rates change everyday but I'll promise you two things; I'll tell you the truth and I'll do the best I

can. My office phone number is 925-465-1223. You can also reach me by email at patrick@beyondtherate.com.

See you next time for a short conclusion. I'd like to wrap this series up with a few brief words and hope you'll join me for one last episode of the "Beyond the Rate" podcast series. Stay tuned.

Bye for now.