POLITICS & GOVERNMENT

The Politics of Complexity

THE SOURCE: "District Complexity as an Advantage in Congressional Elections" by Michael J. Ensley, Michael W. Tofias, and Scott de Marchi, in ***The American Journal of Political Science***, Oct. 2009.

Ideologically driven gerrymandering over the past several decades has produced an increasing number of relatively homogenous congressional districts represented by legislators with little to fear from most challengers.

But anyone who thinks more diverse districts are rough-and-tumble rings of fierce political competition has another thing coming. Political scientists Michael J. Ensley of Kent State University, Michael W. Tofias of the University of Wisconsin, Milwaukee, and Scott de Marchi of Duke University write that in districts where the political landscape is especially hard to understand, potential challengers rarely materialize, and when they do, they are more likely to lose.

The trio gauged the complexity of congressional districts by examining opinion-poll data on residents' views on economic issues such as taxation and on cultural questions—what to do about abortion, guns, and school prayer. Districts where the two areas of belief were highly correlated have "simple" political landscapes; a candidate in such a district can make accurate predictions about how constituents feel about gun control based on how they feel about taxes. In districts where people have, say, uniformly conservative economic views but heterogenous social values, potential challengers face a problem. In these "complicated" districts, putting together an accurate picture of people's views requires a lot more polling than in a simple district (a process that can be quite expensive).

The 2000 election bore out the authors' argument. In districts with greater political complexity, a serious challenger was far less likely to emerge, and those who did fared much worse come Election Day. In the ever artless language of political scientists, "If we compare a district with a complexity score two standard deviations below the mean to a district with a score two standard deviations above the mean, there is a 2.5 percent difference in the incumbent's expected share of the vote." Simply put, the more complex a district, the better the incumbent fared. Ensley and colleagues explain, "By definition, an incumbent has done a good job of finding a successful platform at least once." Best of luck to the go-getters who want to throw their hats in the ring.

ECONOMICS, LABOR & BUSINESS

The Wrong Fix for Foreclosures

THE SOURCE: "Reducing Foreclosures" by Christopher L. Foote, Kristopher S. Gerardi, Lorenz Goette, and Paul S. Willen, in ***Research Review***, Jan.–June 2009.

One solution to the recent surge of foreclosures has gained a lot of currency: Rewrite the lousy mortgages that are the source of this mess. It's a win-win plan: Borrowers would keep their homes, and banks would save money they would have lost in foreclosure. Sheila Bair, chairwoman of the Federal Deposit Insurance Corporation, has estimated that this strategy could prevent 1.5 million foreclosures. Since each foreclosure is estimated to cost the lender an average of $120,000, total savings could be as much as $180 billion. At the end of September, 14 percent of the nation's borrowers were either delinquent or in foreclosure. But loan modifications just aren't happening at the rate one would expect. Why not?

A new study by Christopher L. Foote and Paul S. Willen of the Federal Reserve Bank of Boston, Kristopher S. Gerardi of the Federal Reserve Bank of Atlanta, and Lorenz Goette of the University of Geneva shows that rewriting the terms of mortgages nearing foreclosure would be bad business for banks. The reason is two-fold: Banks would be overly inclusive and rewrite mortgages that wouldn't have gone into foreclosure; and of those they would rewrite, many

Boarded up and vacant homes are an all too common sight in Gary, Indiana, where foreclosures outpaced sales through the end of 2009.

would go into foreclosure anyway.

Foote and his colleagues found that foreclosures are not being driven chiefly by exorbitant interest rates or other qualities of the mortgages themselves. They point instead to what they call the "double-trigger": the interaction of an "income shock"—a job loss—and falling home prices. "Consider a borrower who has lost his job. No permanent modification can make the house affordable if the borrower has no income." Moreover, "when the value of the house that collateralizes the loan is falling," the servicer who delays foreclosure risks an even larger loss in the future.

To test their theory, the authors tweaked data covering more than half of the U.S. mortgage market. What happens if mortgage debt rises as a percentage of people's incomes? What if more borrowers are unemployed? For each variable they altered, they could see the effect on payment delinquency. What they found is that even a 10 percent increase in the ratio of debt to income that a borrower takes on at the start of a loan increases the risk of a 90-day delinquency by only seven to 11 percent. In contrast, just a one-percentage-point increase in the unemployment rate raises the probability by 10 to 20 percent. Worst of all, a 10-percentage-point fall in house prices raises it by more than half.

Some economists have contended that banks have been slow to modify loans because it's very complicated to do so with mortgages that have been sold and repackaged in securitized bundles. But Foote and his colleagues found that securitized and non-securitized loans have been modified at about the same rate.

The authors argue that it's a mistake for Washington to focus on making it easier to modify loans. Rather, it should create a bridge for people who have recently lost their jobs to help them get through the rough patch without losing their homes.

ECONOMICS, LABOR & BUSINESS

Ditch the Dollar

THE SOURCE: "The Dollar and the Deficits" by C. Fred Bergsten, in ***Foreign Affairs***, Nov.–Dec. 2009.

When Chinese officials began talking openly last year about the possibility of unseating the dollar as the world's reserve currency, they got the brushoff from Washington. But C. Fred Bergsten, director of the Peter G. Peterson Institute for International Economics, argues that that was a mistake. After nearly a century, the dollar's role as the world's dominant currency is no longer in America's national interest.

It may make Americans feel good that everybody needs greenbacks to do business in the global economy, but the costs to the United States have grown very high. China and other nations game the system by keeping the value of their currencies artificially low relative to the dollar, allowing them to sell their goods more cheaply in the United States while hamstringing U.S. exports. Then they pour the vast dollar holdings they've amassed into the United States, providing easy money that fosters government deficits, high-risk mortgages, and debt-fueled consumer spending—key elements in the recent boom and bust.

In 2006, the U.S. current account deficit (which includes interest and other money flows in addition to trade in goods and services) topped $800 billion, a