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The Problem and Promise of Credit in American Life

Finance is always social. It is social not just because it distributes profits and risks among people, but also because those profits and risks are distributed on the basis of understandings, usually unspoken, of what people can imagine owing to and sharing with one another.

This insight is so foundational as to perhaps seem trivial, but it often gets lost when people talk in the technical language of finance: of liquidity, risk profiles, and asset classes. That technical language, useful for understanding the dynamics of capital flows, frequently obscures the social character of finance and keeps us from considering another vital set of questions we might ask: Why do people consider a given system reasonable in the first place? How do groups decide what they owe to one another as members of a community or nation?

In the broadest sense, this book is a sociological excavation of finance. It seeks to unearth the logics buried under jargon and taken-for-granted assumptions. To do this, American Bonds traces the historical evolution of two powerful, behind-the-scenes forces in U.S. credit markets, securitization and federal credit programs, from the founding era through the 1960s. The book’s core contribution is to show how early American land and housing policy gave rise to a wide-reaching politics of credit allocation in the twentieth century. It makes the case that U.S. government officials have long used landownership, housing markets, and easy credit as policy tools, and that they have done so in an elusive search for not only ways to avoid the redistribution of wealth while still ensuring widespread economic opportunity, but also ways to effectively govern within a remarkably complex and fragmented political system. It is a history with implications for how we think of America’s underappreciated developmental state, its market-heavy social policies, and its volatile financial systems.
The Background and the Cases

The backdrop for this story is the sheer historical magnitude of America’s real estate markets. Already by 1890 nearly half of U.S. households were owner-occupied, and a staggering four-fifths of farming households headed by people over the age of 60 were owner-occupied. Such high levels of homeownership required a massive amount of credit to circulate, and in the right way: not just among businesses, but among families; not just in cities, but in rural areas; not just among the well-off, but among ordinary people; not just in the short term, but long enough for families to pay off the sizable debt. This was no easy feat, as other scholars have noted. Mortgages are risky and costly transactions, ones that many banks avoided, either partially or completely, for long periods of time. Especially in the nineteenth century, moving the nation’s capital reserves from eastern centers across a vast frontier into the hands of small borrowers was a challenge. In earlier eras, as now, lenders could glut a market with credit amid a speculative fever. America’s mortgage markets—centered on the most economically and emotionally significant debt held by ordinary families—were also endemically unstable and inefficient.

American mortgage markets are therefore old, expansive, morally supercharged, and highly consequential. All of this is ideal for a study of the social life of finance. Mortgage markets’ long and troubled history also provides a context in which to understand the two cases at the heart of this book: securitization and federal credit. Both evolved as ways to manage the risks and costs associated with lending and, in so doing, improve the flow of credit across the nation. Mortgage markets are therefore at the center of the analysis that follows.

To say that mortgage markets are at the center of this story is not to say that this book is exclusively concerned with mortgages. Credit circulates, and so do lending techniques. Following developments in securitization and federal credit back through U.S. history means periodically addressing domains like farming, commercial real estate, and railroads. Furthermore, a key lesson of this book is that credit is a multipurpose political tool. Every chapter describes how people use credit to solve their problems, decisions that are shaped by the challenges of governance within an institutionally fragmented political system. American Bonds therefore covers a great deal of ground even as it returns to the matter of mortgage markets and to the question of how securitization and federal credit moved money into them.

WHAT IS SECURITIZATION?

Securitization is a financial technology that repackages loans for resale. Just as undesirable cuts of meat can become more appetizing when combined into a sausage, loans can be made more desirable to investors by being combined in a
pool that diversifies those loans’ risks. Bonds can then be issued that give investors a share of the pool. Alternatively, a large loan or asset, like the mortgage for a skyscraper, can be divided up and sold in smaller pieces, as certificates or bonds. To extend the culinary metaphor, the key issue becomes who gets the prime cuts (the rights to the first repayments, or senior debt) and who gets the offal (that is, subordinated debt that only pays out after other classes of bondholders are paid).

In today’s securitization markets, sellers pool assets within special purpose entities (that is, trust or shell companies) in order to remove those assets from their balance sheets. Complex financial formulas then determine how the expected income from those assets will back bonds that bear different levels of risk. When those pools are made up of mortgages, the bonds are called mortgage-backed securities. The financial engineers who design these pools typically arrange for some kind of credit support that ensures certain bondholders will get paid even if the assets in the pools, like mortgages, default. Examples of credit support are insurance policies purchased from another company or guarantees from a governmental agency.

In short, securitization is a way of reselling existing loans. As such, it is part of a secondary market. The primary market is where the loans are first issued. Robust secondary markets boost primary markets because they attract new customers and provide existing customers with more ways to raise funds. Anyone who has purchased a car expecting to one day resell it or trade it in has experienced this process at work.

Securitization is a revolutionary technology, best known for the role it played in the turn-of-the-millennium housing bubble. Bolstered by a friendly regulatory environment, computing power, and new information technologies, the mortgage securitization market went through explosive growth in the 1980s. Soon every kind of debt—school loans, auto loans, credit card obligations—was securitized. Financiers boasted that this represented a breakthrough in risk management. It was to be a new era of credit access for poorer borrowers, constituting nothing less than the democratization of credit. As investors came running from around the world, the banking industry reshaped itself around securitization. Economists Greenwood and Scharfenstein estimate that as the boom was reaching its peak between 2000 and 2006, “all of the incremental growth in household credit as a share of GDP [gross domestic product] was securitized.”5 Sales slowed but did not stop after the market crashed. In 2016, an average of $210 billion worth of securitization issuances were traded daily.6

Why study historical iterations of the securitization market? Long before our current market emerged in the 1960s, the United States had major mortgage bond markets in the 1830s, 1870s, and 1920s. This book uses these earlier markets to analyze the different social logics of securitization; it is, to
my knowledge, the first book to do so. This book also uses securitization’s political history to better elucidate the relationship between states and markets. Most people associate revolutionary financial technologies with private entrepreneurship. As historian Louis Hyman writes, however, this world-changing version of securitization “began with the federal government.”

Quasi-governmental mortgage dealers Fannie Mae and Freddie Mac built the market in the 1970s and 1980s, and remain powerful forces in it today. Even before then, in the 1960s, government offices used securitization to sell off government-held loans as a way to raise off-budget funds. Those sales point to an even larger story. It was not just any part of the government that incubated securitization: it was the federal credit programs.

WHAT ARE FEDERAL CREDIT PROGRAMS?

Federal credit programs direct and promote the flow of credit in the economy. Today the U.S. federal government reports that it owns $1.3 trillion in loans and guarantees another $2.5 trillion through a web of credit programs embedded within a range of governmental agencies. That combined total of $3.8 trillion, accumulated over decades, is nearly as large as the entire $4 trillion reported federal budgetary expenditure for 2017. The total for federal credit jumps to $8.5 trillion if you include in the calculations other obligations like the guarantees offered by Fannie Mae and Freddie Mac (which remain under government conservatorship but are excluded from the budget because they are officially privately owned entities) or the Federal Reserve’s holdings of mortgage-backed securities acquired after the 2008 meltdown. As economists Mariana Mazzucato and Randall Wray note, around a third of all privately held debt in the United States is backed in some way by the federal government. And even that impressive amount is not a full account of government support for credit markets. Add tax expenditures that encourage lending, and the extent of government credit support gets even larger. Between 2005 and 2009, the period that covers the apex of the millennial housing boom, the mortgage interest deduction amounted to a $434 billion incentive for borrowing. None of this even touches on efforts of state and local governments. Federal credit programs are not, therefore, the entirety of government credit support in the United States, but rather an institutional center for such efforts. As such, they have something to teach us about the role of credit in the American political economy.

The actual federal credit programs take many forms: some issue loans, some provide guarantees and insurance, and some buy and sell existing loans. They are also old: nineteenth-century credit support helped build roads, railways, canals, western irrigation systems, and more. Credit programs operate across policy domains: the Commodity Credit Corporation (CCC) uses loans to subsidize farmers; the U.S. Agency for International Development
(USAID) gives loans to other countries as a form of foreign aid; the Federal Emergency Management Association (FEMA) and the Small Business Association (SBA) provide loans as a mode of domestic disaster relief. Through its credit programs, the federal government has bolstered nearly every sector of the economy, with extensive backing harnessed for core industries: first agriculture, then housing, and most recently education. Credit programs are not just financial conduits. They are also institution builders. The Federal Farm Loan Act (FFLA) promoted the use of the long-term amortizing mortgage. The SBA underwrote the early venture capital industry. The Export-Import Bank pioneered certain kinds of overseas lending.

Despite their importance, large gaps remain in our knowledge of how these programs developed. Existing research glosses over the nineteenth century or looks narrowly at specific sectors rather than how the programs operate as a group. In some cases, scholars analyze credit programs as instances of something else, like industrial policy, governmental partnerships, or Progressive Era politics. While I owe a great debt to this research, much of which I draw on throughout this book, major questions about the history and implications of federal credit, as a mode of policy in its own right, remain unanswered. We know little, for example, about the rise of credit as a tool of statecraft in the United States or the ramifications of this for developmental or social policy. Scholars like Susanne Mettler, Christopher Howard, and David Freund have called for a more in-depth examination of federal credit allocation. This book takes up that call.

WHY STUDY SECURITIZATION AND FEDERAL CREDIT TOGETHER?

Securitization and federal credit programs have repeatedly influenced one another’s development. The chapters that follow will show that early government credit support for rail and roads pulled settlers across the continent and helped turn the United States into an agricultural powerhouse. Western settlement drummed up demand for credit on the frontier, where brokers used securitization to facilitate farm lending. As these efforts failed, populist farmers concluded that a stronger central government was their best chance for securing regular access to cheaper credit, a shift in political opinion that enabled the total overhaul of the farm credit system in the Progressive Era, a policy that in turn set precedents for the New Deal. In the postwar era, the credit programs incubated the modern securitization market. When lawmakers used securitization to boost the nation’s struggling mortgage markets, they set the course for a revolution in American mortgage markets.

This back-and-forth between federal credit programs and securitization can teach us something. It is indicative of how private and public actors work
together and over long periods of time to build markets, even within the supposedly laissez-faire-friendly context of the United States. As an examination of the role of states in markets, *American Bonds* extends a long line of research into how governments make modern capitalist markets possible.\(^{16}\) This body of scholarship has already shown that modern states and markets grew up together. Healthy markets generate a tax base that funds governments, and governments in turn help markets thrive by providing stable property rights, developmental policies, official currency, regulations, risk protections, and emergency protections.\(^{17}\)

Financial markets are a core part of this history of state–market relations, because financial markets are special public goods. Finance is the seat of money and credit, of national savings, capital, profits, and reinvestment. If financial markets are inefficient, money trickles when it should flow. If financial markets are unfair, capital gathers in one part of the system at the expense of the rest. If financial markets are rapacious—too fraudulent, corrupt, or speculative—bad debts accumulate like an infection in a bloodstream. Because finance circulates through various other markets, government efforts to ensure its proper functioning can have far-reaching ramifications. Greta Krippner has shown that government efforts to manage the flow of money and credit sparked America’s transition to a new era of financial capitalism in the 1970s and 1980s.\(^{18}\) She is one of many scholars whose work reveals that U.S. federal involvement in markets is far more expansive, and generative, than typically appreciated.\(^{19}\) *American Bonds* contributes to this effort by showing how America’s complex political system influenced the way that the U.S. federal government historically engaged with credit allocation.

The paired cases of securitization and federal credit also provide a multidimensional look at the morality of financial markets. At no point did securitization represent a pristinely rational approach to risk management. Loan pools are essentially little moral worlds: they require decisions about who belongs and who is excluded, who gets profits and who bears losses, who is allowed to exit the deal and under what conditions. Their design reflects how people conceive of their financial relations and obligations to one another. While securitization is useful for understanding these little moral worlds, the federal credit programs illuminate the big moral world of political economy. A mortgage pool of loans from the Veterans Administration (VA) issued with government guarantees is not just a contract between a borrower and a lender, but a bond between a borrower, a lender, and a larger community that now bears the risks associated with its soldiers’ loans. The process for reallocating or issuing credit involves decisions about which groups or businesses are too important to go without access to capital and which ways of lending are preferable.

Here the analysis follows the lead of sociologists like Viviana Zelizer, Bruce Carruthers, and Marion Fourcade, who analyze exchanges as part of the
process through which people understand, define, and negotiate their social connections. Financial markets are part of how we delimit the role of the government in credit markets and that of credit markets in society. They help determine the extent to which Americans must use market exchange to meet fundamental needs like housing, education, and healthcare; they also help determine the degree of social support available within the realm of market exchange. Those decisions are never just about potential economic returns; they are also about national priorities and values.

In all, the paired histories of securitization and federal credit provide complementary perspectives on how credit allocation operates at the center of the U.S. political economy. By showing how specific practices entail judgments about who should get what, the book illuminates some of the social logics behind who gets profits and who gets risks in American credit markets. And by showing how lawmakers turn to land and credit to solve a host of political problems, this book situates housing and credit within a larger pattern of political fragmentation and conflict that goes back to the earliest days of the nation. It is to that larger context the chapter now turns.

A Fractured Nation

A key contention of this book is that U.S. housing and credit policies operate within a larger context of governmental complexity. That context has been detailed by scholars of American political development, a field that explains how the nation’s core political institutions have developed over time.

The U.S. government is sprawling and fragmented by design, a result of the founders’ decision to balance the authority of the central government with that of individual states. This dispersion of political power has led to the development of a government with nearly 90,000 units spread out over the nation’s states, counties, cities, towns, special districts, and school districts, as William Novak notes. At the center of this sprawl is a political core made up of the three branches of the federal government, whose powers are balanced against one another’s. The complexity is reproduced within each branch. The two chambers of Congress work through a welter of committees, 20 in the House and another 21 in the Senate. The judicial branch is divided into three levels and 94 federal districts, all of which are “naturally passive” because their power is only activated externally. The Department of Justice alone includes 40 offices that share law enforcement authority with other entities like state troopers, county sheriffs, military police, and immigration and customs enforcement officers. This structure has resulted in competing seats of authority and a veritable gauntlet of veto points that any policy must run.

All nations have groups with varied interests that clash, but the United States, because of its sheer size and complexity, creates more opportunities for
conflict than most. The most brutal of the divisions that give rise to such conflict are America’s racial divides, institutionalized through slavery, Jim Crow, and mass incarceration, which compromised American democracy in the past and continue to fester today. In the nineteenth century American racism intersected with hardening regional divides that increasingly separated the industrial North, the Cotton South, the wheat- and cattle-filled Great Plains, and the timber- and produce-rich West Coast. These cleavages were the foundation for distinct economies, lifestyles, and worldviews that became an existential threat to the nation in the lead-up to the Civil War. Today, a mix of geography, economy, culture, and race mark an increasingly hostile gap between “blue” coastal elites and the “red” heartland. Other divides cut across space: the separation of the haves and have-nots, of gender and ideology.

This combination—fragmented political institutions that overlay complex social divides—defines American political life. When polarization is especially high and interest groups are strong, the structure can result in gridlock, or even devolve into what Francis Fukuyama has called a “vetocracy,” in which groups use veto points to grind government to a halt. Scholars like Michael Sandel and Gary Gerstle have similarly observed that this highly fragmented system can only work given some basic agreement about shared goals and rules for political discourse. Without that basic agreement, paralysis results. Political scientist Eric Shickler points out that even at its best, the American political structure forces the kinds of compromise that do not bring consensus so much as they produce lingering dissatisfaction, since, by definition, none of the negotiating parties get exactly what they want. To make matters worse, since those advantaged by a previous agreement have an interest in protecting their gains, new rules tend not to replace previous arrangements so much as overlap with or modify them. Shickler concludes that the American style of pluralism is particularly “disjointed.”

Political and social fractures did not stop the federal government from growing, but they did change how it grew. Government officials devised ingenious ways to avoid veto points, link various seats of power, and generally compensate for the system’s shortcomings. While they are almost always used in some kind of combination, for analytical clarity it can help to group these diverse policies into three types: partnerships, inducements and incentives, and market forms. These work-arounds, which are summarized in figure 1.1 and table 1.1, are regularly incorporated into government entitlements, regulations, and subsidies.

Partnerships are collaborations with local governments and private entities, either to design or to implement policy. With Damon Mayrl, I have written about the various forms these collaborations take, from simple contracts (as when the federal government hired a subsidiary of Halliburton to build holding
The Policy Work-Arounds

**A. Partnerships**

- **Work-Around Example:**
  - A Partnerships U.S. federal government charters the nonprofit Red Cross to provide rehabilitation to veterans after the First World War.
  - ab Partnerships with incentives/inducements AmeriCorps is a public–private partnership. Its Segal Education Award program offers forgiveness for direct government loans for AmeriCorps members who later work full-time for eligible nonprofits and government agencies and make payments for 10 years.

**B. Incentives and inducements**

- Tax deductions for charitable giving
  - bc Market-based inducements and incentives The UNICOR Federal Bonding Program provides theft insurance for businesses that employ former inmates.

**C. Market forms**

- FEMA uses cost-benefit analyses to evaluate hazard-mitigation projects.
  - ac Market-based partnerships U.S. federal government charters the for-profit Federal National Mortgage Association to promote the nation’s secondary mortgage market.
  - abc Incentives built into market-based partnerships Small business set-asides give preferred access to government purchases and contracts to businesses owned by women, people from disadvantaged backgrounds, and service-disabled veterans.

**Table 1.1. The Policy Work-Arounds**

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<tr>
<th>Work-Around</th>
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<tr>
<td>A Partnerships</td>
<td>U.S. federal government charts the nonprofit Red Cross to provide rehabilitation to veterans after the First World War.</td>
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<td>ab Partnerships with incentives/inducements</td>
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cells in Guantanamo Bay) to complex hybrid organizations that share control and costs (like port authorities). Inducements and incentives direct private individuals and companies toward desired actions. Tax breaks encourage people to buy homes, have children, save for retirement, or donate to charity. Inducements like high-occupancy vehicle lanes encourage carpooling. Increasingly, inducements are taking the form of subtle “nudges.” For example, by switching a government program to one that people must opt out of (rather than opt in to), the government can increase rates of participation in programs; this strategy has been used to provide more retirement benefits to veterans and more school lunches to low-income children. Often the ability to partner or trade with the government is the incentive, such as when priority for a government contract goes to companies with a good safety compliance record.

Market forms entail the application of market tools in political spaces. They include strategies with origins in market spaces and market techniques that privilege efficiency over core political logics (like rights), such as the use of cost-benefit analyses to evaluate government programs. To some extent, the use of market forms derives from the government’s long and frequent use of partnerships. Sometimes partnerships are with nonprofits, but frequently they involve alliances and contracts with for-profit businesses and firms. Researchers have observed a global rise in market forms under neoliberalism, but this book will focus on earlier historical iterations.

These work-arounds have multiple political advantages. Partnerships circumvent veto points and avoid jurisdictional battles by shifting authority and expenses into private hands. Inducements and incentives minimize expenses. Tax expenditures are overseen by revenue committees, which makes them easier to implement than programs routed through the veto-ridden appropriations process. Nudges use the power of modern behavioral science to manipulate people into voluntarily making choices the government wants them to make. Richard Thaler and Cass Sunstein defend the approach as “a relatively weak, soft, and non-intrusive type of paternalism” that people tend to prefer to regulations that are openly restrictive, involve punishments or fines, or cost more money to enforce. By directing markets, government officials can appease constituents without openly redistributing resources through taxation and spending.

Partnerships, incentives, and market forms all recruit citizens into the work of governance. Some scholars see them as a kind of colonizing power that constitutes an underappreciated strength of the U.S. federal government. State power can be measured not just in terms of centralized control, but in generalized influence. Viewed this way, the federal government’s capacity to branch out—to incorporate private groups in the rule of law and to seed desired action rather than just take it—is not a sign of the administrative weakness of the central government, but a measure of the state’s considerable breadth of reach.
The political advantages of policy work-arounds come at a cost, however, because they aggravate the underlying issue of government complexity. Suzanne Mettler warns that inducements and market forms “obscure the role of government and exaggerate that of the market.” Steven Teles calls the resulting morass of policies a “kludgocracy” in which “an army of consultants and contractors” with an interest in creating ever more complex programs further gums up the political works. Elisabeth Clemens has compared the American state to a Rube Goldberg machine, “an immensely complex tangle of indirect incentives, cross-cutting regulations, overlapping jurisdictions, delegated responsibility, and diffuse accountability.” Within this tangle, complex policies wrap around core institutions like vines covering a trellis.

Land, housing, and credit have always been part of this complex web of American statecraft. The distribution of land is a relatively straightforward aspect of this entanglement: the public domain was a resource that the national government could distribute in lieu of taxing and spending. Even when the land was cheap or free, its distribution had ramifications for national credit markets because people still needed to borrow to build and farm. Credit did not just support land policy, however. Because credit fuels growth, it has long been a favored market form in its own right. A closer look at the politics of credit can clarify why.

The Political Lightness of Credit

Credit can generate growth. It gives borrowers access to funds and goods today based on a promise to repay the debt, with interest, in the future. Borrowers can use these funds to buy things, which raises demand, or build and sell things, which increases supply. Economic historian William Goetzmann has called credit a “time machine,” arguing that this ability to turn expected future values into current resources did nothing less than make modern civilization possible. The political usefulness of credit as such a time machine has not been lost on lawmakers. Across generations and party affiliation, officials have realized that carefully orchestrated engagements with finance can please constituents, save tax dollars, and avoid political gridlock. I use the metaphor of lightness to convey the many levels of political flexibility credit entails and how this has mattered in American political life.

Credit programs are fiscally light. They can yield big results for low costs. Guarantees of loans do not require expenditures when issued; as contingent liabilities, guarantees only result in a charge if a borrower defaults. Direct loan programs are more expensive at the moment when money is lent but nevertheless offset expenditures by generating income through fees or repayments or by selling off government-held loans. Furthermore, credit programs can be easily set up as partnerships, with shared financing costs and reduced overhead,
which makes them administratively light. Entities like the Commodity Credit Corporation or Fannie Mae straddle governmental boundaries: they can be just private enough to stay off the federal accounts (since they issue their own debt and so are not funded through the Treasury) but public enough to follow government mandates and receive special support.43

Credit programs also have a kind of budgetary lightness. Budgets determine the rules of the game for government spending, which makes them powerful disciplinary institutions to which officials continually orient themselves.44 Inconsistent and improper accounting among the federal credit programs has obscured their costs in official accounts, allowing the government to raise and spend off-budget funds; accounting in these programs was not modernized until the 1990s, and watchdogs warn that official numbers still understate the programs’ activities.45 Subsidies within the programs, like below-market interest rates, cost the government money but, like tax expenditures, do so in the form of money-not-collected.

The abstract nature of credit facilitates this lightness. For all that credit is tied to some of the most concrete parts of life—actual dollars used to buy real objects—the debt is itself simply an agreement. Credit is a promise that money exchanged will be repaid, an obligation extended over time.46 As a promise, it has no preexisting organic or material state. Rather, people create systems to organize, record, track, and enforce borrowers’ obligations and lenders’ rights. That characteristic of credit—its role as a space of classification, a thing defined in the last instance through processes of accounting and categorization, trust and commitment—can be powerfully harnessed in political contexts. Credit markets, because they deal in promises over time, are highly sensitive to questions of legitimacy, trust, and reliability. Governments, when they are stable and not in crisis, are specialists in legitimacy, trust, and reliability.

New theories of state power allow for deeper understanding of this elective affinity between politics and credit markets. At the center of modern governments, writes sociologist Pierre Bourdieu, is “the production and canonization of social classifications,” a special capacity that he calls “symbolic power.”47 As the word “canonization” indicates, a government does not create these understandings of state classifications out of whole cloth, but rather puts an official stamp on existing notions. Official stamps matter because the authority and power behind them can be transformative. Government support for currency, for instance, is what allows money to be readily and widely exchanged.48

When it comes to credit markets, governments have many options for using their symbolic power to induce desired outcomes. Some of these options are classic forms of regulation. Adjustments to banking rules (like requirements for holding reserves) or to the Federal Reserve’s open market window are among the best known of such strategies and generally work in broad strokes, influencing the overall level of credit and money in the economy. The credit
programs, in contrast, more readily work like precision instruments and direct credit exactly where the government wants it to flow.

A theory of symbolic power also clarifies how credit programs came to have a kind of ideological lightness. Credit programs give government officials a great deal of rhetorical leeway because they combine market forms with partnerships and inducements and are used for many purposes. Historian David Freund found that designers of the New Deal housing credit programs talked about them as “essentially non-interventionist” efforts that “unleashed” private capacities. A 2016 special budgetary report on credit and insurance introduces the programs as both a response to market failures and a means of combating inequality. This polysemy is useful for lawmakers, who must answer to multiple audiences with conflicting agendas. With Damon Mayrl, I have argued that government officials’ ability to manage such understandings is an important part of policymaking.

One lesson from this book is that credit’s ideological lightness was not inevitable. While existing research tends to take for granted that Americans like markets and so like credit programs, that assumption neglects how frequently people are offended by any sort of boundary transgression. Indeed, the boundaries between states and markets are especially fraught. Many nineteenth-century Americans rejected national government involvement in credit markets as a corrupt and paternalistic form of overreach, an understandable stance given the rampant patronage politics of the day. Progressive reformers did not just build a modern civil service; they also reframed federal government credit support as a form of self-help and set a path for the more expansive use of credit as a tool of statecraft that developed during the New Deal.

There are political costs to credit’s political gains. Notably, guarantee programs save on immediate expenditures but can be costly in cases of default. Credit programs also miss out on revenue: they socialize risks of loans while letting private firms keep the profits from repayments. There are also organizational trade-offs associated with credit programs. These programs frequently compromise administrative transparency, coordination, and control. Moreover, the act of pumping out loans and guarantees is inflationary, which was not an immediate problem in the New Deal, when economic growth was so desperately needed, but became a major concern in the 1960s. Then, with inflation high and money tight, economic advisors lamented that credit programs undermined their attempts to cool the economy.

Despite these political and organizational trade-offs, the overall advantages of federal credit for lawmakers and bureaucrats are considerable. Under the right conditions, credit distribution promises growth without costs, without appearing to redistribute wealth, and without the polarizing specter of government overreach. Credit allocation can seem like a mild kind of policy even as it boosts entire industries. Viewed this way, it is not surprising that lawmakers
have so often used credit allocation to manage tough distributional issues and veto points—or that, as a result, credit programs emerged as a key part of America’s complex style of statecraft.

Credit and America’s Peculiar Developmental State

I have argued that government officials use credit to navigate the rocky terrain of American politics. But what does this mean for how we think about the U.S. economy? Today’s massive securitization industry speaks to how credit policies can impact global markets. It is only one example of many. The chapters that follow will also show that credit programs are not intermittent, marginal, or even limited to addressing flaws in credit markets. Credit programs have historically supported everything from railroads and farming to housing and energy. Credit has been used for disaster relief, foreign policy, and military efforts. It has been integral to the promotion of amortized mortgages, overseas lending, venture capital, and more.

In making this point, *American Bonds* brings credit allocation to the fore of our understanding of U.S. government officials as creative and consequential market participants. In the field of sociology, Fred Block and colleagues have argued for the existence of a U.S. “developmental network state” that works through brokerage and research funding. The support by the Defense Advanced Research Projects Agency (DARPA) of the early Internet is a quintessential example of the world-changing capacity of government brokerage and research support. Economist Mariana Mazzucato builds on this insight to argue that the American government should be thought of as a visionary entrepreneur that specializes in long-term investments for innovations with low early returns and high risks—the kind of big gambles that scare away private investors but open up new markets. Most of the significant technologies used in the iPhone, she notes, trace back to some government effort to fund or facilitate the innovation. Legal scholars Robert Hockett and Saule Omarova refer to the mass of government economic subsidies and investments as the “developmental financial state.”

The United States never had a developmental state akin to that of a nation like France or Japan, where the growth of specific markets was subject to extensive centralized planning. But it is also true that American markets grew with considerable help from the state. The extent of U.S. government support for the economy is larger than most people realize. This is nowhere more consequential than in the housing sector. The website of the Federal Housing Administration (FHA) boasts that the agency is the world’s largest mortgage insurer, having backed 47.5 million properties as of 2017. Half of U.S. residential mortgages outstanding today were connected in some way to Fannie, Freddie, or the Federal Home Loan Banks. In times of crisis,
when the normal government programs are combined with bailout efforts, the level of government support of markets can reach jaw-dropping proportions. In 2009, the special inspector general for the Troubled Asset Relief Program testified to Congress that the total potential liability of the U.S. federal government through its various guarantees and bailouts in a worst-case scenario amounted to $23.7 trillion—the equivalent of 150 percent of that year’s GDP.60

Block’s theory of a developmental network state argues that U.S. developmental policy is generative rather than controlling, reliant on bottom-up change instead of top-down direction. A look at credit allocation bears this out. Political economist John Zysman studied European industrial policies and found that activist industrial governments used financial systems as “the muscle and the apparatus” to move an economy.61 In France and Germany, governments used their influence over a centralized banking system to ration credit. Zysman concludes that “the single discretion necessary to all state-led industrial strategies” is credit allocation.62 He further notes that such a strategy necessarily failed in nations like the United States where robust capital markets allowed companies to circumvent government attempts at credit rationing through banks.

Zysman is right about the importance of credit for economic development, but he misses the potential effectiveness of decentralized credit policies. Historically, the U.S. government continually induced change in domestic markets, but its credit distribution was diffuse, like a sprinkler, rather than streaming from a main source, like a spigot. Continual recalibrations to U.S. markets were made through the decentralized network of the credit programs. The modern securitization market stands as an example of how that approach can work. Credit is a valuable policy tool everywhere, but the use of that tool is shaped by particular political and economic contexts. In nations where political life is more centralized, so too is governmental credit allocation.

To be clear, I am not arguing that government officials are exclusively responsible for the growth of U.S. credit markets, or even the rise of the modern securitization market. On the contrary, the book is full of examples of nongovernment actors making important breakthroughs, not the least of which are private companies’ efforts to develop securitization deals in the postwar era, discussed in chapter 9. My point is rather to contribute to scholarship that moves creative government activities in markets from the margins to the center of the story. To clarify how government officials have mattered is not to say that private firms have therefore been inconsequential, but to paint a more detailed picture of how markets are made. A focus on government actors at key junctures yields a more detailed account of how government officials work with and alongside nongovernment actors to build an economic world.
Land, Homes, and Credit as Social Policy

Land and housing programs have long served as America’s functional equivalent of a European welfare state. Political scientist Laura Jensen argues that nineteenth-century land distribution was effectively a welfare program used to placate and provide for the population. Land distribution was an early entitlement, especially for white male veterans. Housing scholars like Schwartz, Kemeny, and Castles have posited a trade-off between homeownership and welfare programs, making the case that the U.S. government directed family savings over the life course through credit and tax policies that promoted homeownership.

America’s market-friendly social policy is not just a story of land and housing, but also one of easy money and credit access. Gunnar Trumbull has observed that in the early twentieth century, American labor saw consumer credit as a safety net for striking workers and so forged a pro-credit political coalition with a hypercompetitive banking industry eager to branch into consumer markets. In a sweeping historical analysis, Monica Prasad argues that nineteenth-century farmers inadvertently set the United States on this path when they promoted a progressive tax system that ultimately failed to fund a more expansive welfare state. An underfunded welfare state combined with a pro-consumption bias (farmers wanted policies that encouraged people to buy their produce, after all) to create political support for cheap credit. The key insight here is that robust consumer credit markets and weak welfare states can be reinforcing systems: in the absence of a stronger welfare state, American families latched on to credit as a lifeline, which created pressure for government officials to ensure its supply.

If credit can substitute for social policy, it is because credit programs can do many of the things that welfare programs do: smooth consumption and cushion families during emergencies, compensate for low wages, and secure cardinal resources like housing, healthcare, and education. While credit provides economic support through lending, it does not follow that all of its benefits are repaid with interest. If the government issues a loan at a below-market interest rate, this is a subsidy. So too if the government forgives a loan or allows someone to refinance on easier terms, that is money in the bank for recipients.

When it comes to its use as a mode of social policy, credit’s ideological lightness means that recipients of federal credit are protected from the dishonor sometimes associated with welfare programs. That is because credit is a market form and so comes without the stigma associated with charity. But while a program like Social Security is not stigmatizing because someone has already paid into it, that arrangement is flipped with credit programs: borrowers get the payment first and repay it later. Instead of accumulating...
dishonor, the borrower builds a credit history and has a chance to become an owner of a home or business. In this way, credit programs provide status and enhance financial citizenship. The open obligation of the credit form—the fact that there is repayment—helps people overlook the various opportunities and subsidies also transferred through this process. Subsidies and state assistance then appear to be forms of self-help.

Credit and Racial Inequality

The government’s extension of its symbolic power through credit has frequently been politicized along racial lines and used in racially exclusionary ways. Examples of credit’s role in upholding white supremacy run throughout this book. Before the Civil War, southern congressmen sought to protect the national balance of power that ensured the entrenchment of slavery by denying credit support for western infrastructure development, and southern states guaranteed mortgage bonds that included slaves as human collateral. After the Civil War, southern states used strict lending laws to lock in a system of labor controls and debt peonage that hit black farmers first and hardest. After the New Deal, credit programs thrived while efforts at European-style centralized planning failed, in part because southern congressmen did not see credit programs as a threat to white supremacy.

Racist credit politics were never just a southern issue, of course. Perhaps the most famous example of the national scale of these practices is the Federal Housing Administration’s insurance program that helped many families who had no credit record secure their first mortgages. This was a crucial boost, because it gave families a chance to build wealth that could be tapped in emergencies or old age, or be passed along to later generations. In the postwar era, these government-insured mortgages overwhelmingly went to white families. As political scientist Chloe Thurston has argued, people of color excluded by the housing credit programs fought for inclusion in them from the creation of those programs. There is a large body of research that shows how the exclusion of families of color from the housing credit programs created lasting differences in wealth, as well as differences in access to the best public schools and job opportunities.

When families of color were excluded from the largesse of the housing programs, they lost out on multiple fronts: the chance to build what became the main form of wealth for American families, access to higher-quality schools in tax-rich suburban neighborhoods, the chance to build a credit record on forgiving terms, and a chance to get all of this support in a way that was entirely divorced from the stigma associated with receiving welfare. Historian David Freund has investigated the legacy of New Deal housing credit programs and concluded that these programs’ racial policies had lasting implications for the
nature of northern white racism. With the contributions of the credit programs downplayed as mere market corrections, white families saw their resulting sprint up the social ladder not as an achievement made easier through credit hoarding, but as deriving exclusively from their hard work and so signifying their virtue and deservingness.\textsuperscript{72}

If credit is a time machine, it is not only dollars that flow through it: credit continually carries forward the prejudices and inequalities of the past. There has been no time period or region in which credit distribution has not been distorted by racism. Here, then, is another way we can think of the lightness of credit policy: as historically serving the interests of white Americans.

**Distribution in America**

It is by looking at economic and social policy together that we can grasp the overall implications of the use of land and credit as a mode of distribution in the U.S. political economy. The real payoff of these strategies is the promise that accompanies them of not needing much social policy at all: the acceptance of the idea that market growth should alleviate poverty and, with it, the need for redistribution. Lizabeth Cohen has studied the postwar era and concluded that suburban consumerism became a civil religion because “it promised the socially progressive end of economic equality without requiring politically progressive means of redistributing existing wealth.”\textsuperscript{73} Greta Krippner has investigated the financial turn of the 1970s and 1980s and found that lawmakers used financial deregulation to avoid openly rationing resources (lawmakers preferred that “the market” take responsibility for hardship).\textsuperscript{74} Scholars like Wolfgang Streeck, Colin Crouch, and Raghuram Rajan have all observed lawmakers around the world using easy credit to compensate citizens for low wages and frayed social safety nets in the era of neoliberalism.\textsuperscript{75}

By tracing the history of securitization and federal credit programs over a long time, this book connects these insights and clarifies the overarching pattern of their development as it played out in the context of American history. Federal credit is an important tool of statecraft, one reaching back to the earliest days of the nation. It has always been implicated in distributional politics. The meaningful change from the nineteenth to the twentieth century was the extent to which lawmakers approached credit allocation as a backstop or primary lever. Viewed this way, the government’s involvement in the securitization market is not surprising, but typical, and typical not just of housing policy, but of an array of credit policies—credit policies that are in turn typical of the use of markets as one facet of the generally complex style of American statecraft.

The contribution of this book is not just to make sense of credit’s role in the U.S. political economy, but also to illuminate how the social logics of distribution operate within credit markets. We see this operation in the distinct
historical approaches to the design of mortgage bonds. Populists built cooperative protections for borrowers into their loan pools. A century later, government-guaranteed mortgage bonds reflected the social logic of the credit state, in which state-promoted financial development and risk redistribution served as an alternative to wealth redistribution.

The point here is an extension of an old insight within economic sociology: financial tools are designed by human beings who grapple with concrete problems imbued with political pressures, historical contingencies, and shared understandings. Culture and politics are always the material out of which people come to understand their interests and desires, and develop strategies for pursuing them. Social life is not like soft flesh covering an underlying, bone-hard economic truth. It is the marrow. It is the stuff from which economic life is built.

**Researching Credit Politics in Time**

This is a work of historical sociology that draws on existing research to theorize social processes. The method follows what Theda Skocpol has called the “targeted primary” approach, which draws from secondary materials and supplements them with original research to fill in details as needed. In this case, reports from the Progressive Era informed my analysis of the emergence of the Federal Farm Loan Act, and original archival research clarified early government use of securitization for asset sales. As the title indicates, *American Bonds* is exclusively a study of the United States, so it does not include systematic comparisons with other nations. That said, I hope this study generates knowledge that will be useful to other scholars who make such comparisons, and chapter 10 will consider why we might expect some of these relationships to matter elsewhere.

Paul Pierson has noted that analyses that cover long time spans are ideal for identifying relationships between systems of institutions, which may unfold slowly or unevenly over many years. An approach that necessarily trades depth for historical breadth, the long view is well suited for a study of the relationship between American political institutions and credit markets, one of this book’s primary goals. Methodologically, this book also borrows from Jeffrey Haydu’s insight that institutions are instances of iterative problem solving, which means scholars can approach them as both elements to connect and cases to compare. This study applies the same logic to financial techniques: I analyze how new financial tools create resources and problems that influence later groups, and I treat financial tools as objects to compare in order to better understand social logics of exchange that are hard to see in isolation.

The analysis starts with a watershed land policy in the founding era. It ends with a 1968 regulatory change that reorganized the housing credit program Fannie Mae and authorized it to trade in government-guaranteed
mortgage-backed securities. The year 1968 is a reasonable end point because it marked a key policy transformation: the nation was leaving behind an older New Deal system and turning toward a new one organized around securitization, the system still in place today.

While I will briefly examine the effects of these shifts on later events in chapter 10, the book does not cover in detail the millennium-era housing boom that so famously implicated securitization and Fannie Mae in the economic collapse of the first decade of the twenty-first century. Instead, it analyzes the older, less well-studied roots of that market. *American Bonds* is not a history of the recent housing and credit crisis, then, but a prehistory of that crisis. To the extent that those deep structures persist, it is perhaps a prehistory of crises still to come.

**Looking Ahead**

The chapters that follow compare different modes of mortgage finance over time, paying special attention to the interaction of political institutions and mortgage markets. Because the book links financial technologies to their broader social contexts, some chapters emphasize large-scale historical transformations, while others look more closely at specific markets.

The first half focuses on the volatile world of nineteenth-century mortgage finance. Chapter 2 traces the development of the nation’s patchwork mortgage market and early crisis-prone credit programs. The latter include land-sale-on-credit schemes intended to raise funds to pay down Revolutionary War debt, as well as the controversial, crisis-prone railway programs. Chapter 3 begins at the end of the nineteenth century, as the problem of credit provision reached a boiling point, and compares three approaches to pooling loans from this period to show how they articulated competing visions for a rapidly changing political economy. Failures at this time set the stage for future credit programs. Chapter 4 shows how Progressives returned to the issue of farm credit distribution in the early 1900s and drew on European precedents to reframe credit allocation as a way for the central government to help people help themselves. Chapter 4 also shows how political conflict shaped the development of the federal farm loan system, a breakthrough in allocative credit that set precedents for policies to come.

The second half of the book focuses on the explosive rise of both residential mortgage markets and federal credit in the twentieth century. Chapter 5 shows how, as the United States transitioned from an agricultural to an industrial nation, mortgage lenders promoted homeownership as the new measure of independence, success, and virtue. This chapter also discusses how a growing federal government in World War I took new steps into housing policy. Chapter 6 takes a close look at the postwar boom in mortgage bonds, this time made up
of smaller slices of large mortgages for commercial buildings like skyscrapers. The market heated up at the close of the 1920s as lenders marketed mortgage bonds to families. The collapse of this market in the early 1930s wiped out the private market for mortgage bonds completely and led to regulatory prohibitions against small-investor purchases of mortgage bonds.

The New Deal brought the creation of Fannie Mae and other housing credit programs, and also heralded a much broader expansion of credit as a tool of statecraft. This is the focus of chapter 7. Here we see how government officials used the ideological and fiscal lightness of credit allocation to find a more palatable, but still effective, alternative to European-style economic planning. Chapter 8 reviews the evolution of federal credit programs in the postwar era into a sprawling, decentralized system with housing at its center. Chapter 9 shows how that system incubated securitization, and how that in turn helped set the terms for the reorganization of housing finance in 1968. The analysis shows how budget politics can shape the type of credit policies that are crafted. The concluding chapter discusses how the events recounted throughout the book help us understand the housing bubble of the early 2000s. It also draws lessons for sociological theories of states and markets.

Considered together, these chapters show how political institutions shape government participation in markets. They reveal how competing moral visions of the American political economy are written into specific ways of pooling and dividing loans. And they detail how Americans have repeatedly turned to land, housing, and credit in an elusive search for widespread economic opportunity that comes without the attendant costs of political conflict, financial risk, or large-scale redistribution. The chapters present, in other words, the enduring problem and promise of credit in American life.
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