

The Mortgage Corner

Government doesn't Want Fannie, Freddie to Succeed

By **Harlan Green** / Special to CASA

AT A TIME WHEN THE HOUSING MARKET IS JUST BEGINNING TO RECOVER, the US Treasury wants to close down Fannie Mae and Freddie Mac, the two GSEs under government conservatorship.

Counselor to the Secretary for Housing Finance Policy Dr. Michael Stegman, speaking at Monday's National Council of State Housing Agencies Legislative Conference, stated: "I know that many of you want to know where we are on housing finance reform. On this subject, let me be clear: the Administration stands by our belief that the only way to responsibly end the conservatorship of Fannie Mae and Freddie Mac is through legislation that puts in place a sustainable housing finance system that has private capital at risk ahead of taxpayers, while preserving access to mortgage credit during severe downturns."

But Timothy Howard, chief economist and a senior Fannie Mae executive for 23 years, counters, "Fannie Mae never experienced a threat to its solvency because of difficulty rolling over its maturing debt, nor did it need to sell assets at depressed prices to survive. The company never experienced a market crisis. At the time it was put into conservatorship, Fannie Mae's capital significantly exceeded its regulatory minimum."

So dissolving Fannie and Freddie makes no sense for several reasons. There is no financing model that has yet been created to replace their securitization structure that in effect guarantees almost all conforming and Hi-Balance conforming loans, which account for more than 60 percent of loan originations today.

And, they are generating immense profits for the US Government that has commandeered all of their profits since a 2012 amendment to the 2008 conservatorship agreement. "As of last December, the Treasury had received a total of \$225.4 billion from the companies," wrote *NYTimes* Columnist Gretchen Morgenson. "An additional \$153.3 billion in receipts from Fannie and Freddie could be generated through fiscal year 2025, according to estimates in the 2016 budget offered by the president."

So why does the government want to close them down when their sometimes too strict underwriting standards have brought loan default rates back to

historical levels, and have repaid more than the \$186 billion lent to them?

The quick answer is that our government fears they may have to bail out the GSEs again, putting taxpayers at risk in some hypothetical future with their current structure as stock holding corporations, but with an implicit government guarantee that they can't fail.

Treasury officials (and the banking lobby) also maintain it gives them an unfair interest rate advantage that has enabled them to keep lower capital reserves, and thus a lower expense overhead, therefore impeding the development of so-called "private-label" mortgages generated by commercial lenders, but not guaranteed by the GSEs.

This is double talk. Morgenson highlighted the ongoing debate on whether Fannie and Freddie should be re-privatized in describing a lawsuit by a major stockholder of the GSEs whose stock is in effect worthless, unless the government allows them to rebuild their equity: "The problem with the apparent involvement by Treasury and White House officials in the decision to commandeer Fannie's and Freddie's earnings is that by congressional statute, the F.H.F.A. is supposed to be an independent agency, tasked by law to protect the safety and soundness of the companies. Letting the companies' profits flow to the Treasury had the opposite effect. Allowing them to rebuild their capital with profits after they repaid the taxpayer seems more like it."

Howard also thinks Fannie and Freddie can still function as viable institutions. "The argument for bringing Fannie Mae and Freddie Mac out of conservatorship and using an amended version of them as the basis of the future mortgage finance system is extremely straightforward: their credit guaranty mechanism is low-cost, efficient and effective, and has a proven track record of success."

Do we need any other reason to break the gridlock that has kept the GSEs in conservatorship, now that the housing market is recovering? Their model works, and without them the housing market would be in far worse shape.

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