Putting our Housing Finance System on a Sustainable Path

BIPARTISAN POLICY CENTER

What's wrong with the status quo?

Too much public sector involvement

- 99 percent of mortgage-backed securities (MBS) issued in 2012 were backed by the federal government [a]
- 87 percent of mortgages originated in 2012 were backed by the federal government [b]

Too much taxpayer risk

- Government currently takes first loss (and all loss)
- Insufficient capital reserves are being set aside to cover losses from a potential drop in house values and foreclosures

Lack of private sector involvement in bearing credit risk

- Private label security market remains very small ($13.4 billion in 2013 [c])
- Private sector credit risk absorption limited to small, experimental risk-sharing transactions and multifamily market

Prolonged uncertainty chokes off the flow of credit

- In 2013, the average FICO score for a Fannie Mae-backed loan was 753; 755 for Freddie Mac [d]
- Compared with 2001, up to 1.2 million fewer purchase mortgages were made in 2012 due to tighter credit availability [e]

The GSE model is flawed

- Private corporations with publicly traded stock and an implicit government guarantee did not work
- This model does not promote alignment of incentives by all parties in the mortgage chain

How does Johnson-Crapo solve these problems?

Streamlines public sector role

- Creates independent Federal Mortgage Insurance Corporation (FMIC) that limits federal involvement to explicit government backstop
- Provides strong regulation and oversight of the housing finance system

Sets out clear taxpayer protections

- Requires 10% first-loss coverage on all MBS, from guarantors or capital markets
- Fee on mortgage payments set aside in Mortgage Insurance Fund for catastrophic risk, providing further buffer before the Treasury and taxpayer are exposed

Provides prominent private sector role in mortgage financing and bearing credit risk

- Private sector takes the first-loss credit risk
- Establishes a Securitization Platform owned and operated by private sector members
- Leaves loan origination, aggregation, first-loss coverage, and servicing to the private sector

Lays out a roadmap for a stable, liquid mortgage market and broad credit availability

- Creates uniform securitization agreement for government-backed securities
- Supports and maintains the To-Be-Announced (TBA) market
- Promotes continued availability of 30-year fixed-rate mortgages

Eliminates the GSE model with an orderly wind-down

- Winds down Fannie Mae and Freddie Mac over at least a 5-year transition period
- Provides for alignment of interests among all parties in the mortgage chain

Sources

[a] Inside Mortgage Finance, “Mortgage and Asset Securities Issuance,” 2013.

[b] Inside Mortgage Finance, “Mortgage Originations by Product,” 2013.

[c] Inside Mortgage Finance, “Mortgage Originations by Product,” 2013.

[d] Fannie Mae 2013 Credit Supplement (February 2014) and Freddie Mac Fourth Quarter 2013 Financial Results Supplement (February 2014).

[e] Laurie Goodman, Jun Zhu, and Taz George. “Where Have all the Loans Gone? The Impact of Credit Availability on Mortgage Volume.” The Urban Institute, March 2014.