The Daily Dish

The Coming Housing Risks

DOUGLAS HOLTZ-EAKIN | JULY 11, 2022

The big economic issues of the day are inflation and recession risks. But beneath the sturm und drang about these issues, a host of other pressing policy issues remains concerning pharmaceutical pricing reform that retains innovation incentives, international tax rules that support growth and not confiscatory taxes, and…taxpayer risks from the housing market.

That's right. The greatest hits of 2007–2008 are back: Fannie Mae, Freddie Mac (the government-sponsored enterprises or GSEs), housing market risks, inadequate capital, and the risk of taxpayer bailouts. The starting point is that the outlook for both residential and rental housing shades negative, in large part because the strategy employed by the Federal Reserve will have a disproportionate impact on housing.

But the regulatory environment is layering on new risks. Despite 14 years under the conservatorship of the Federal Housing Finance Agency (FHFA) "each Enterprise remains undercapitalized." Despite this, the FHFA just moved to relax the capital requirements. Worse, the FHFA announced it would require Fannie and Freddie to put in place Equitable Housing Finance Plans that would (shocker) aim at advancing equality in housing markets. For example, they would deploy a "special purpose credit program" that would assist African American borrowers with down payments. Typically, the 20 percent down payment is the responsibility of the homebuyer, or some of the capital risk is taken by private mortgage insurance. This approach takes capital that is supposed to protect taxpayers to subsidize home purchases by borrowers who simply don't have the financial preparation to do so.

This is the classic GSEs-FHFA two-step. Stretch the risks that the GSEs can take and they make more money – until things go bad and the taxpayers pick up the tab. At the same time, this would steal the market share of private-sector housing finance firms. Fortunately, at least some members of Congress are paying attention. As reported by *Politico's Morning Money*, 10 members of the House wrote to FHFA Director Thompson, noting "The Enterprises have a history of venturing into new activities and product offerings that go well beyond their congressionally approved roles in the secondary market. The FHFA must do more to ensure there is appropriate transparency regarding any new products or activities that the Enterprises undertake and that these activities do not displace private firms or crowd out private capital."

Fortunately, there is something that can be done. As the congressmen note, Thompson could "finalize the long overdue rulemaking on Prior Approval of Enterprise Products, which was proposed in October 2020 and would ensure there is adequate oversight and transparency around new products and activities the Enterprises bring into the market. This is a statutory requirement under Section 1123 of the Housing and Economic Recovery Act of 2008 and has yet to be met over a decade later."

Nobody is opposed to greater equity in economic activities. But to pursue it by deliberately disregarding the lessons of recent history, doing a U-turn on regulatory stringency, and inviting another tranche of taxpayer bailouts is likely to make *everyone* worse off.