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# Experts paint a private capital market for regulators

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The situation in housing finance today is that taxpayers fund and guarantee more than 90% of new mortgages through Fannie Mae, Freddie Mac and government agencies.

But housing experts testifying [3] in front of the Senate Committee on Banking, Housing and Urban Affairs expressed a desire to revamp the system quickly.

Mark Willis, resident research fellow at **New York University Furman Center for Real Estate and Urban Policy** firmly believes it’s time to let the jumbo market stand on its own without a government guarantee.

After all, the jumbo market accounts for a quarter of the dollar volume of mortgages per year and more than 8% of all mortgages by unit count.

"While it may in the end make sense to trim back further the share of the market eligible for the government wrap, opening up the market above $417,000 should provide a very significant opportunity to attract private, credit-risk-taking capital," Willis said in a prepared testimony before the Senate Committee.

Once the jumbo private securitization market is functioning at scale, it will be possible to evaluate the impact of any further lowering of the limits for the private sector to begin to serve the vast bulk of the mortgage market, which lies below $417,000.

"If there is no significant difference in what private, credit-risk-taking capital proves willing to finance in the jumbo market compared to the existing offerings in the conforming market, then further testing of the right level for the loan limit should be undertaken," Willis explained.

The current government-sponsored enterprise mortgage-backed securities market provides trillions of dollars of financing to the mortgage industry. Additionally, government guarantees and other structural features are required to maintain this market.

Thus, collateralized guarantee in the form of credit-lined notes could be used to reduce the risk to taxpayers from government provided guarantees on MBS, said Andrew Davidson, president of **Andrew Davidson & Co., Inc.**

As a result, the so-called "securitization cooperatives may be the best form of organization and risk sharing. The existing GSEs could be transformed into originator-owned cooperatives with little disruption to the mortgage finance system," Davidson explained.

The transformation would be relatively straightforward, he said.

"Fannie Mae and Freddie Mac could be transformed into cooperatives, first by stripping out the unnecessary and unwanted functions, such as the retained portfolios, and by lowering loan limits and limiting loan types," Davidson said.

He added, "Fannie Mae and Freddie Mac could also utilize risk sharing transactions to reduce their risk exposure. The stripped down entities could then be sold to qualified cooperatives that would be subject to appropriate levels of regulation."

With the appropriate government guarantee in place, the TBA market could continue unchanged through the transition of the GSEs from conservatorship to cooperative ownership.

The alternative to implementing any type of proposed restructuring is to wait for reform until there is agreement over the end point — something that Capitol Hill has been discussing for the past five years.

The longer the conservatorship continues, the more likely it is that it becomes permanent, said Phillip Swagel, professor at the **University of Maryland**.

"Such a nationalized housing finance system is a default outcome if no reform is undertaken," he concluded.

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