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Will Fed's Paper Spur Momentum for Housing Fix?

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By Donna Borak

WASHINGTON - A recent paper by economists at the Federal Reserve Board on ways to fix the housing market has reinvigorated the debate over the issue among key policymakers.

While the paper did not make concrete recommendations, instead analyzing the various options and challenges in the housing market, it appears to have jumpstarted discussion of the issue.

"It underscores to me - they get it; that if we don't have a housing recovery, the economic recovery is going to be at best modest and slow and we need to do something," said Brian Chappelle, a partner at Potomac Partners, a consulting firm that specializes in mortgage finance. "They've really been the honest broker in this debate."

The move has drawn criticism from some Senate Republicans, including Sen. Orrin Hatch of Utah, who argued the central bank went beyond its dual mandate of price stability and maximum employment. But analysts and others said it is not unusual to have the Fed weigh in on the issue given its overall importance to the economy.

The central bank also did not pick sides in the ideological divide between the political parties on the issue, instead detailing the complex task policymakers will have to take on.

"The paper actually goes a long way to demonstrate how difficult it is to come up with any solutions," said Brian Gardner, a political analyst with KBW Inc. "They actually go through different policy options and show where some of the hurdles are when they talk about refinancing and getting beyond the [government-sponsored enterprise] GSEs."

Still, some saw signs of frustration in the move, noting that Fed officials have been increasingly outspoken on the need to revive the housing market.

"The housing sector has not contributed to the recovery," Fed Gov Elizabeth Duke said earlier this month. "I do believe that forceful and effective housing policies have the potential to significantly influence the speed and strength of our economic recovery."

Unlike other economic periods, housing is unique in becoming a drag on economic growth. Combined with a poor labor market, issues such as an excess supply of vacant homes, less access to mortgage credit, and ongoing costs from an inefficient foreclosure process continue to hamper Fed efforts to promote a stable economy.

"The message from the big Fed paper is we need to do something because there is no magic bullet," said Gardner, a former Capitol Hill staffer.

To be sure, the Fed's paper avoids specific recommendations by the central bank - purposely so. "Our goal is not to provide a detailed blue print, but rather to outline issues and tradeoffs that policymakers might consider," the paper says.

But the paper may prove an impetus - and political cover - for other actions by the government.

"The Fed has laid the ground work for the administration to do more, and the ball is now in the court of the President to then decide what those next steps will be," said Jaret Seiberg, senior policy analyst for Guggenheim Partners' Washington Research Group. "In our view, a broader refinancing initiative has to be on the agenda because it works politically and economically."

Analysts say the first step in that process will be to see exactly what settlement is reached between the state attorneys general and the top mortgage servicers.

"The government is going to do what the government is going to do; but if the industry thinks that's a reasonable settlement, that the penalties and the requirements fit the crime, then I think we can move forward and address the issue the Fed's paper talks about," said Chappelle. "However, if the industry believes the penalties far exceed the crime, [in other words] instead of a slap on the wrist they're getting repurchase demand for hundreds of thousands of dollars per loan - that to me is the next major milestone in this process."

At the very least, the paper has proven effective in helping restart a debate that has remained stalled since the Obama administration released an options paper last February on possible ways to reform the housing finance system, analysts said.

"In the context of what the Fed is trying to achieve - a conversation among policy makers - it's a good start," Chris Low, chief economist for FTN Financial, wrote in a note to clients.

But others argued the central bank felt compelled to take this step because it had been ineffective lobbying behind the scenes.

"To some extent, some might see this as a signal of the strength of the Fed putting pressure, I see it almost as a failure," said Mark Calabria, a former Republican staffer on the Senate Banking Committee and director of financial regulation studies at the **Cato Institute.** "We've worked the back channels with [acting director of Federal Housing Finance Agency] DeMarco. We've really tried to jaw bone him into doing more. We've really tried to jaw bone Congress into doing more, but they won't listen to us, so we're going to put out a policy paper and try to build support for it."

Fed officials have not publicly said whether there has been any coordination with the FHFA or the White House, which has been working on a plan to revitalize the housing market, including a possibly massive refinancing proposal.

But observers suspect that is the case

"There are more back channel discussions between the Fed and the Treasury and the administration, then I think people generally realize," said Bert Ely, an independent analyst based in Alexandria, Va. "It's not kosher to do, but in fact, it happens. I wonder to what extent they got some kind of blessing. We're not going to give you any cover, we're not going to affect anything you do, but we certainly wouldn't mind seeing it out there."