AEI's Wallison, Hudson's Weicher Discuss Housing Policy and the Fincl Crisis

By Robert Feinberg

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The Cato Institute hosted a presentation April 7 by Peter Wallison, Financial Policy Studies Fellow of the American Enterprise Institute, of this book Hidden in Plain Sight: What Really Caused the World's Worst Financial Crisis and Why It Could Happen Again, about the role affordable housing goals imposed on Fannie Mae and Freddie Mac played in the financial crisis of 2008.

At the same event, John Weicher, director of the Hudson Institute's Center on Housing and Financial Markets and author of Housing Policy at a Crossroads: The Why, How and Who of Assistance Programs, offered his own views on government-sponsored enterprise (GSE) regulation, recalling the reluctant efforts of the Department of Housing and Urban Development to regulate the GSEs while Weicher served there under President Reagan and Secretary Jack Kemp. He found that the GSEs had been investing in subprime mortgages largely independent of the affordable housing goals.

Wallison's main thesis is that the affordable housing goals set by Congress and the Clinton and Bush administrations beginning in 1992 helped to fuel the housing bubble that was financed with mortgage-backed securities whose value collapsed and led to the rescue of financial institutions that had invested heavily in those securities. He contends that the Dodd-Frank Act of 2010 was an inappropriate response because it wrongly blames the Wall Street banks, rather than faulty housing policy, for the crisis and it subjects the largest banks to burdensome regulations that cripple their ability to lend.

Wallison argues further that the financial crisis episode of 2008 followed a lengthy period of stability in financial markets and if Dodd-Frank were repealed or substantially amended, this would help the markets return to their natural state of quiescence.

He added some intriguing reflections on his experience as a member of the Financial Crisis Inquiry Commission, a panel of six Democrats and four Republicans that was set up by Congress to study the 2008 crisis. He lamented that Dodd-Frank was enacted six months before the Commission completed its work, that Chairman Philip Angelides had complete control over the hiring of staff and that the other Republicans on the Commission declined to sign his dissent, perhaps because it criticized the George W. Bush administration in which two of them served.

This writer has expressed astonishment the Obama administration, and the Bush administration before it, joined by Wallison and others, have propounded the narrative that the financial crisis was an aberration due to the collapse of mortgages provided to borrowers who could not make the payments. This writer tried to alert the Reagan transition of the looming crisis in 1981, and episodic crises and bank failures have proceeded fairly continuously since the early 1970s.

Instead of taking action to contain the crises, virtually none of the legislative fixes has been implemented and the size of the embedded losses has grown to an unknown, untold figure that almost certainly exceeds the GDP. In this writer's view, the next crisis episode is being forestalled by quantitative easing and the continued support of financial markets by the Treasury and Federal Reserve. The potential for another episode to occur whenever the authorities withdraw support or miscalculate is why this debate continues to rage, with high stakes attached to it, as reflected by market gyrations as investors speculate as to whether and the Fed will move to raise interest rates.