Seeking to Reinflate the Housing Bubble

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ITEM: *"Regulators want to ensure mortgage lenders retain some of the risk on loans they originate, as it is crucial to strengthen the housing finance system, a top Treasury official said on Friday," reported Reuters for June 24.*

ITEM: *"The Obama administration is 'seriously considering' a proposal by bank regulators that could cause mortgage rates to rise on all but the safest home loans, a Treasury Department official is set to say Friday," reported Dow Jones on June 24.*

ITEM: *"The Obama administration is exploring ways to support rental housing as the troubled U.S. real estate sector has kept potential buyers on the sideline, a top U.S. Treasury official said Friday," reported Reuters for June 24. Under Secretary Jeffrey Goldstein "said the administration's range of options to expand support for lending for multifamily rental properties include reforms such as risk-sharing with private institutions."*

ITEM: *Federal Reserve Chairman Ben Bernanke "said the Fed was trying to help the housing market by leaning on the banks it regulates to modify loans 'where appropriate,'" reported Reuters on June 22.*

ITEM: *The Obama administration, reported the Wall Street Journal on June 22, "has said it intends to end the risk to taxpayers by laying out options that would wind down the [government-sponsored Fannie Mae and Freddie Mac mortgage companies] and build a private mortgage-finance system."*

ITEM: *Nearly "two years after the recession officially ended," the New York Times commented on May 24, "the housing market is still in trouble." "Selling and building of homes are one of the economy's most powerful engines," said the editors of the Times. "Until the market recovers, the entire recovery is imperiled. Falling home equity dents consumer confidence, making things worse. Since the problems are not self-curing, a government fix is in order. But the Obama administration's main antiforeclosure effort has fallen far short of its goal to modify three million to four million troubled loans."*

CORRECTION: The same folks who brought you the managed housing economy that tanked want to continue to serve as the mismanagement.

This time, we are promised, it will be different. Sure. Rather than allowing the marketplace to sort matters out, federal regulators want to preside over everything from what they consider to be the right amount of risk for mortgage lenders to how much "affordable" housing should be built to how large a subsidy is given to certain renters — all accomplished with a multiplicity of federal sticks and carrots.

We taxpayers are to foot the bill even as we pay off the billions upon billions of dollars lost from previous regulatory blunders. *The New York Times*, the presumptive "newspaper of record" and paragon of left-wing thought, assures us that Washington must handle the prescriptions because the problems are not "self-curing" — proving that a foolish opinion can be shared with millions of people and still be drivel.

Who is to say what should be the appropriate price for housing? A level that is bad for sellers is likely good for buyers. Whether widgets or homes are involved, assuming the market is allowed to move, folks tend to buy more at lower prices and less at higher prices; suppliers tend to produce more when prices are higher and less when prices fall. If the government doesn't allow the forces of supply and demand to work, trouble is virtually guaranteed.

Borrowers and lenders are dealing with the same forces — unless, that is, the government decides for political reasons to fix, say, the

mortgage market so lenders will assume what would otherwise be unacceptable risks.

In his 2009 book, *The Housing Boom and Bust*, economist Thomas Sowell correctly pointed out that problems took off when trying to fix a problem that really did not exist — a supposed nationwide shortage of “affordable” housing. Some of this, he noted, was based on the proclaimed concern for poor and minorities that produced a drive to override traditional mortgage standards. However, in the end, Sowell observed, it was “by no means clear that the poor or minorities came out ahead at all, after the housing boom turned to bust and many were left with mortgage payments they couldn’t meet on homes they couldn’t afford.”

It took the force of government to blow up the housing bubble that has since thudded to earth. Sowell writes: “Lenders did not spontaneously begin to lend to people who would not have qualified for loans under the traditional criteria that had evolved out of years of experience in the market. Such risky loans were made under growing pressures from government regulatory agencies and politicians, and even threats of prosecution from the Justice Department if the statistical profiles of borrowers whose loan applications were approved did not match the government’s preconceptions.”

It didn’t take a soothsayer divining animal entrails to predict what would occur. As even the liberal *Washington Post* has admitted — albeit years too late — the “oversubsidization of homeownership” by the government-sponsored entities (GSEs) Fannie Mae and Freddie Mac led to catastrophic losses. It might be accurate to say, opined the untimely Post, “that federal housing policy has helped destroy communities.”

The part played by the Clinton administration, among others, is covered in a new book written by Gretchen Morgenson and Joshua Rosner, *Reckless Endangerment*. It recalls that President Clinton promised how the government’s assistance in homeownership would boost the economy. Rather, “in just a few short years, all of the venerable rules governing the relationship between borrower and lender went out the window, starting with … the requirement that a borrower put down a substantial amount of cash in a property, verify his income, and demonstrate an ability to service his debts.”

When Uncle Sam interferes with the marketplace, it makes little difference if his motives are pure. In the case of lax mortgage lenders, the fallout included more risks being taken; additional losses down the line; distortions in the market, with long-term negative effects; and a degrading of lending standards.

The cut-rate ride promised a gold ring. It begat corruption. Columnist Mona Charen has summarized some of the players and their actions:

> Fannie Mae lied about its profits, intimidated adversaries, bought off members of Congress with lavish contributions, hired (and thereby co-opted) academics, purchased political ads (through its foundation), and stacked congressional hearings with friendly bankers, community activists, and advocacy groups (including ACORN). Fannie Mae also hired the friends and relations of key members of Congress (including Rep. Barney Frank’s partner).

Currently, Fannie and Freddie are in conservatorship. Nevertheless, they continue to write about 90 percent of all new mortgages.

The Obama administration and some on Capitol Hill now say they want private companies to take over many of the roles the GSEs have been playing, yet they continue to try to give special favors to Fannie and Freddie over their would-be private-sector competitors. There is also a separate bipartisan “compromise” piece of legislation that would get rid of the two agencies and create five more in their place with somewhat different rules, but which would continue to leave taxpayers on the hook.

Regulators still want to give renters more supposed assistance, though they have hardly been ignored to date. Mark Calabria of the Cato Institute estimates that the federal government, through the Department of Housing and Urban Development, has spent close to a trillion dollars in this area, meaning that the federal taxpayer has paid “enough to outright buy almost a third of all rental housing.” However, as a study explained in *Real Estate Economics*, only about a third of that money has benefited the renters directly, with the balance going to developers, owners, and others.
Much of the federal tinkering these days is aimed at driving housing prices to a pre-recession level; doing this, say advocates, will bring up the entire economy. Not so, responds Veronique de Rugy, a senior fellow at the Mercatus Center at George Mason

University, who points out that it makes no sense to try to return to a price level that was a “historic anomaly.” As she writes for *Reason:* “It was only in the last 15 years that prices exploded. The factors behind this sudden change are a mixed bag of government policies that encouraged homeownership and cheap interest rates and a willingness by banks to lend to people who could only realistically afford to pay if housing prices doubled every two years.”

As de Rugy puts it,

> Low prices are not bad for everyone. Yes, low prices are bad for homeowners who are trying to sell and for banks that have lots of bad loans on their books. But low prices are very good for people who want to buy houses. They are also very good for low-income buyers who were priced out of the market in recent years. Finally, low prices are good for people who build homes.
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> But most importantly, only lower prices can address one of the major problems of the real estate market: a bloated inventory of unsold homes.

If the government simply got out of the way, coupled with the abolishment of Fannie and Freddie, it would still take a while for the housing market to clear. But prolonging a correction is no solution.
The economy will certainly not get back on track via more government meddling. As scholar Thomas Sowell has put it: “People used to put money aside ‘for a rainy day.’ But now people who have spent like there are no rainy days are supposed to have the taxpayers pay to give them an umbrella.”

Saying repeatedly that there is a right to a federally subsidized housing loan does not make it so.

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