Opening Statement for Hearing on "The Administration's Report to Congress - Reforming America's Housing Finance Market"
Tuesday, March 15, 2011 at 10:00 A.M. in SD 538

I want to welcome both of our distinguished witnesses.

We are here this morning to discuss the Administration's report to Congress on several possible pathways forward for reforming the housing finance market.

To start off, let me say I am particularly pleased that the report focuses on achieving a better balance in the U.S. housing market to provide for a wider range of housing choices. This includes access to home ownership for those in a position to take on mortgages and a more robust and affordable rental housing sector, which would include something similar to a national Housing Trust Fund, which I created to support and develop affordable rental housing for more Americans.

There is bipartisan agreement that we need to restructure Fannie and Freddie and limit the government's role in the mortgage market. But we have to be careful and get this right, and not rush towards a solution that might not be the right one just for the sake of acting quickly.

Changing the home financing landscape is going to have a major impact on consumers, construction workers, and taxpayers.

If we act precipitously, as some have suggested, the already fragile housing market and the overall economy could be severely affected. The solution, at the end of the day, must be right and actually solve problems, instead of creating more problems.

The proposals we will discuss today outline options to properly target and limit the government's involvement in the mortgage business.

However, we need to clearly remember that the federal government became involved in the housing finance system because of a series of major failures in this sector.

In the 1930s, liquidity risk was born by the borrowers. Back then, a borrower took out a 5-year interest only loan and put 50% of the value of the home down as a downpayment. At the end of the loan, the outstanding balance had to be paid or the loan had to be renegotiated, or rolled over.

During the Great Depression, so many banks went under and borrowers lost so much value in their homes that these loans could not be refinanced or rolled over. As a result, we had a liquidity crisis, and there were massive numbers of foreclosures.

In response, the federal government created the Federal Housing Administration, Fannie Mae, and the Federal Home Loan Banks to help provide liquidity for housing loans.

FHA also standardized a new concept at the time -- 20-year mortgages where the loan would be repaid in full at the end with the FHA insuring lender repayment. Eventually, over time, this lead to the standardization of the 30-year mortgage.

The next housing crisis requiring government intervention was the savings and loan (S & L) crisis.

As interest rates went up to 15%, S & Ls found themselves paying 15% in financing costs, but were only receiving 7% on home loans. This severe mismatch caused many to fail, and the S & L crisis was really an interest rate crisis, which also precipitated a government response.

Fast forward to 2008, to our most recent housing crisis—which many believe was caused by the failure to properly underwrite loans. In other words it was caused by underwriting risk. Lenders improperly believed they had found a way to sufficiently diversify risk through the securitization process that they no longer had to focus as much on the basic and fundamental tasks of ensuring that borrowers could repay the loan at the end of the day. We addressed some of these underwriting issues in Dodd-Frank by, for example, requiring lenders to ensure a borrower's ability to repay and requiring lenders to disclose the maximum a consumer could pay on a variable rate mortgage, with a warning that payments will vary based on interest rate changes.

So, some key questions I will have for our witnesses this morning are: What have we learned from these various housing sector crises? And how can we preserve some of the strengths of our existing system—such as the 30-year fixed rate mortgage, a deep and liquid national mortgage market, and the standardization of mortgage products that has made them attractive for private sector investment—while making our system less subject to such crises in the future?

I am pleased that Chairman Johnson is planning on holding a robust set of hearings on these issues in the months ahead, as we work towards how to best reform our housing finance system and provide access to decent, safe, and affordable housing for all Americans.