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Hearing on Essential Elements of Housing Finance Reform

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Good morning Chairman Johnson, Ranking Member Crapo and Members of the Banking Committee. I'm Jerome Lienhard, president and CEO of SunTrust Mortgage, a subsidiary of SunTrust Banks. Housing finance reform is a critical matter with wide-ranging implications. Thank you for allowing me to participate in the consideration of this important subject.

I am appearing today in my capacity at SunTrust Mortgage and this testimony was prepared after consultation with the Regional Bank Group, an informal coalition of mid-sized lending institutions located throughout the United States. All views expressed today, however, are my own.

SunTrust is headquartered in Atlanta and operates mainly in the Southeastern U.S. We are committed to *Lighting the Way to Financial Well-Being* by listening to client needs and offering a broad range of banking, borrowing, and investment services for individuals and small to-mid-sized businesses.

SunTrust Mortgage, the organization that I lead, is based in Richmond, Virginia and employs about 4,300 teammates. Last year, we originated over $32 billion in mortgage loans which helped more than 120,000 clients purchase a home or lower their monthly payment through refinancing.

The Regional Bank Group consists of 18 financial institutions that share a business model and a set of values dedicated to providing banking products and services to America's families and businesses. We take in deposits and redeploy them by making loans in our communities. Our clients are people and businesses with real needs such as checking accounts, loans and payment services.

Today I'd like to make two important points from the perspective of a regional bank:

- First, while there is a need to reform the housing finance system, it is critical to retain the basic “plumbing” of the system that draws in enormous sums of investment capital and provides borrowers with rate certainty. These features can be retained in a mortgage market that serves the interests of borrowers and taxpayers alike.
- Second, reform must bring more private capital into the mortgage market in a principal loss position without reducing the global demand for mortgage-backed securities and while providing competitive access for small and medium-sized institutions that serve millions of homeowners.

I will spend a few minutes elaborating on each of these points.

Out of thousands of mortgage loans that we make every year, on average, we hold only one in six on our balance sheet. So while we own $30 billion worth of mortgage loans, we actually originated and service more than $140 billion in mortgages involving more than 800,000 households. This is possible for us, and other regional banks, due to the existence of the secondary mortgage market

This vast majority of the mortgages we originate for sale in the secondary market are either “conforming” loans, meaning they comply with the guidelines set by Fannie Mae and Freddie Mac; FHA loans, which comply with the insurance terms established by the Federal Housing Administration in HUD; or VA loans eligible for the Veterans Administration’s guaranty program.

The process by which we price and close the loan and package it for the secondary market are important to a well-informed discussion relating to housing finance reform.

Our clients come to SunTrust Mortgage through our branches, on-line or through our network of loan officers and institutional mortgage partners. We listen closely, assess needs, and thoroughly explain the full range of products that we have available to our clients.

To provide the client with basic information regarding how much they can afford to pay for a house, we must be able to tell them the interest rate and the monthly cost of the loan. You can't buy a house if you don't know what your mortgage payment will be.

We do this by referencing a daily pricing sheet that provides the interest rate and loan terms that can be offered on a guaranteed basis. These prices are set from the price of MBS trading in the "To Be Announced" (TBA) market. TBA security prices assume delivery of conforming mortgages into a Freddie Mac or Fannie Mae mortgage-backed security on a forward basis. The forward-pricing mechanism of the secondary market allows us to lock in the interest rate for clients for up to 90 days.

Once we lock an interest rate, we proceed through the mortgage lending process. Acting as an agent for Fannie Mae and Freddie Mac, we make sure the client's mortgage is properly qualified, underwritten, documented, settled and delivered using GSE guidelines and requirements. This requires expertise and very detailed execution.

But it all starts with the certainty we have regarding how we are funding the mortgage Without that certainty, primary market lenders would be *unwilling and unable* to provide forward price certainty to borrowers. The MBS market solves the "chicken or egg" problem of funding risk by allowing lenders to set mortgage loan delivery terms up front, while allowing execution and delivery to follow.

Through the combination of mortgage standardization and the function of the MBS market, the existing system provides a tangible benefit to borrowers. And these benefits are available for borrowers who transact with originators of any size: local banks, Main Street banks such as SunTrust, as well as the largest mortgage originators.

While there is a need to address taxpayer risk by making structural changes to the housing finance system, the securitization platform, the standard-setting on lending and documentation and the servicing requirements are absolutely essential to maintaining a secondary market. This infrastructure is so foundational that we must emerge from housing finance reform with these key functions intact.

Let me conclude with a few remarks on the critical issue of the structure of the credit guarantee. Our markets perform so well in large part because credit risk associated with mortgage default is assumed by the GSEs. Investors from around the world allocate trillions of dollars of capital to our market because it only involves interest rate risk.

The problem, of course, is that providing credit protection puts taxpayers at risk. Using private sources of capital to cover credit exposure can help alleviate taxpayer risk.

However, if changes are made to the credit guarantee function, it must work well for investors. It must also operate transparently and with scale. The U.S. mortgage market involves trillions of dollars. This quantity of private capital required to backstop the market is very significant. If that market shrinks dramatically, so does lending to borrowers.

We must also consider that if a variety of credit risk devices emerge in place of the relatively simple credit guarantee we have today, it could make mortgage-backed securities difficult for investors to value, fracturing the investor base, reducing liquidity and increasing costs.

To the extent that private capital is intended to stand before any taxpayer-backed guarantees, the entities and instruments must be subject to regulatory oversight. If regulators cannot understand nor keep track of the various risk sharing mechanisms, there is a danger that they will not perform as needed under crises conditions.

Finally, any new source of private sector credit protection should be available for all primary market lenders – including large, small and Main Street institutions. If certain entities cannot obtain competitive access to credit protection in the secondary market, they will have a great difficulty competing in the primary market. Measures that create advantages for the very largest issuers of MBS, or make the cost of market access more expensive for some and not others, will reduce competition and must be avoided. Additionally, any new framework should maximize the secondary market liquidity in the new MBS to ensure that regulated financial institutions are able to participate as investors, use the securities as liquid assets, and pledge them as collateral.

Let me conclude by thanking the Committee again for its time, attention and consideration. We stand ready to provide you with any assistance or advice you may need as your important work continues. I look forward to answering any of your questions.