# MORTGAGE LENDING UPDATE

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# House of Cards

I recently read (actually I listened to it travelling back and forth to work in the car) a book entitled "House of Cards, a tale of hubris and wretched excess on Wall Street" by William D. Cohan. It described the recent events concerning how subprime mortgage loans came to be blamed for our present (It's now over, right? Right?) Great Recession. My ears perked up at the following excerpt, which resonated with me:

"Alone on Wall Street at this time, Whitney (Meredith Whitney, a highly regarded financial services research analyst) had realized that, prior to 1994, home ownership levels in the United States were fairly static at around 64 percent of the population. "That level changed fairly dramatically after 1994," she observed, "when the standards by which an individual could qualify for a mortgage and the required down payment levels became much more liberal. Due to such changes in guidelines, 1.5 million new homeowners were created and homeownership rates rose relatively steeply to 69% where they stand today…The incremental 5% of new homeowners would not have qualified for a mortgage prior to 1994."

…According to conservative Dennis Sewell, writing in the London journal *The Spectator*, one can look to the early years of the first Clinton administration to account for this dramatic-and ultimately quite troubling-increase in home ownership. In 1993, Roberta Achtenberg took the job as Assistant Secretary for Fair Housing and Equal Opportunity at the Department of Housing and Urban Development (HUD). She began implementing the Clinton agenda to "increase home ownership among the poor, and particularly among blacks and Hispanics." Standing in the way of her mission "were the conservative lending policies of banks, which required such inconvenient and old-fashioned things as cash deposits and regular repayments-things the poor and minorities often could not 'provide," Sewell wrote. "Clinton told the banks to be more creative."

Achtenberg set up a series of regional offices, manned with investigators and attorneys, to seek out any discriminatory lending practices among mortgage lenders, with an eye toward prosecuting them if necessary if there was even a whiff of bad behavior. "From the mid 1990s," Sewell wrote, "they began to abandon their formerly rigorous lending criteria. Mortgages were offered with only three percent deposit requirements, and eventually with no deposit requirement at all. The mortgage banks fell over one another to provide loans to low-income households and especially minority customers."

Then there were the changes the Clinton administration made to the Community Reinvestment Act of 1977, whereby banks were rated based on how much lending they did in low-income neighborhoods. "A good CRA rating was necessary if a bank wanted to get regulators to sign off on mergers, expansion, even new branch openings," Sewell wrote. "A poor rating could be disastrous for a bank's business plan." At the same time, the Clinton administration pushed Fannie Mae and Freddie Mac to expand mortgage loans to those who might not have previously qualified for them, and it put into place new rules allowing the two companies to get involved in the securitization of subprime loans. The so-called strengthening of the CRA in 1995 caused an 80 percent increase in the number of bank loans going to low- and moderate-income families…

Sewell saw the direct linkage from HUD's political pressure to the fissure in the credit markets a decade later. "So that's how we get from there to here," he wrote, "from crude attempts at social engineering during the early, heady days of the first Clinton administration to the turmoil on Wall Street."

…Achtenberg…said the goal of increasing home ownership had been a bipartisan effort and pointed to President George W. Bush's American Dream Downpayment Initiative, passed into law in December 2003, which provided up to $200 million to encourage home ownership among low-income first-time home buyers by helping to pay closing costs and down payments…

Other commentators who shared Sewell's conservative political views also shared his analysis. Russell Roberts, for one, a professor of economics at George Mason University, wrote in the Wall Street Journal that in 1996 HUD gave Fannie Mae and Freddie Mac "an explicit target" that 42 percent of their mortgage financing had to be made to borrowers "with income below the median in their area." The targets were increased to 50 percent in 2000 and to 52 percent in 2005…In a separate interview, Roberts said that the 1995 changes to the CRA revised "how it was enforced and it put a wad of power in the hands of community organizations to damage banks that they felt weren't doing enough for poor people. These community organizations became the dispensers of money for zero-down mortgages for poor people, again a lovely thing, but it didn't turn out so well."

…HUD policies dramatically increased the demand for housing and the price of housing, Roberts wrote. "Between 1997 and 2005, the average price of a house in the U.S. more than doubled," he explained. "It wasn't simply a speculative bubble. Much of the rise in housing prices was the result of public policies that increased the demand for housing. Without the surge in housing prices, the subprime market would never have taken off." He rightly pointed out, as had Whitney, that home ownership had increased by the millions. "This was mostly the result of loans to low-income, higher-risk borrowers," he wrote. "Both Bill Clinton and George W. Bush, abetted by Congress, trumpeted that rise as it occurred."

*David Griffin has been financing homes in Macon, Warner Robins and all of Middle Georgia since 1983 and is a member of the Mortgage Bankers Association of Georgia, mbag.org. For an archive of past articles visit mbag.org/ML_Update.htm.(8/11/10)*