FHFA Public Listening Session – Affordable Housing Access
9/14/2020

Operator: Welcome and thank you for joining today's FHFA 2020 Proposed Capital Rule Public Listening Session on Affordable Housing Access. Before we begin, please ensure you have opened the WebEx participant and chat panels by using the associated icons located at the bottom of your screen. Please note that this conference is being recorded and all audio connections are muted, at this time. If you require technical assistance, please send a private chat message to the event producer. With that, I'll turn the conference over to Naa Awaa Tagoe. Please go ahead.

Naa Awaa: Good morning. This is Naa Awaa Tagoe, Principal Associate Director at FHFA. And I'd like to extend another welcome to the Capital Rule Listening Session on Affordable Housing Access. We're delighted to have you join us for this session.

FHFA recognizes that the key component of the enterprises' mission is supporting access to affordable housing for low- and moderate-income families in underserved areas through all market conditions. To this end, FHFA sets duty to serve requirements and affordable housing goals covering purchases of single family and multifamily mortgages for the enterprises.

We really welcome your thoughts on the intersection between the Capital Rule and affordable housing access. I want to extend a special thank you to each speaker in today's session. We appreciate the time you took to write a comment letter and to come here today to elaborate on your comments, to inform FHFA's deliberations on the Capital Rule.

Before we introduce the first speaker, I'm going to turn it over to my colleague, James Jordan, in the FHFA Office of General Counsel to provide some guidelines for this discussion. James.

James: Thanks, Naa Awaa. The purpose of this meeting is to give commenters speakers an opportunity to elaborate on the affordable housing elements of the public comment letters they submitted on the enterprise Capital Rule Re-Proposal, provide input on the comment letter submitted by others, and respond to FHFA questions and clarification on your comment letters.

But FHFA will primarily be in listen mode for the duration of the meeting. FHFA will prepare a memorandum containing a summary of the meeting discussions in your names and organizations, represented as applicable. FHFA also may prepare a transcript of the meeting discussions, including your name and organization's representative. We will timely file the FHFA summary memorandum or transcript along with any documents and materials you've provided to FHFA in the public rulemaking comments docket. FHFA will not discuss the status, timing, or outcome of the rulemaking.

Anything said in this meeting should not be construed as binding on or a formal decision by the FHFA Director or FHFA staff. Any questions that FHFA may have are focused on understanding of views and do not indicate a position of the FHSA staff or the agency. Any gestures such as head nodding or shaking, facial expressions, or verbal expressions, such as yes or okay, made by FHFA staff should not be construed as agreements or

disagreements with points you have presented, and are simply indications that we have heard your points.

And with that, I'll turn it over to our first commenter speaker. Leslie Gooch, at the Manufactured Housing Institute.

Leslie: Thank you to the team from FHFA, Fannie Mae and Freddie Mac, and everyone on the call today. I appreciate the opportunity to share MHI's views during this important listening session. The Manufactured Housing Institute is the only national trade association representing all segments of the factory-built housing industry. Our members include home builders, lenders, retailers, community owners, and managers, suppliers, and others who serve or are affiliated with the manufactured housing industry. We also have 49 affiliated state organizations.

In 2019, the manufactured housing industry shipped almost 95,000 HUD code homes to destinations across the United States, representing about 10% of all single-family housing starts. Manufactured housing offers value to consumers because of technological advancements and cost savings that are associated with the factory-built process. And because of the efficiencies that come with a federal building code, also known as the HUD code. The average cost of a new manufactured home without land is $78,500 compared to the average cost of a new site-built home, which is $297,000 without land.

Manufactured housing is the main source of unsubsidized affordable housing in the country. It is a critical homeownership option, commonly more affordable than rental housing, and it currently serves 22 million people. Moreover, MHI's data shows that manufactured housing residents love living in their homes. MHI recently conducted a national research survey, which indicated that two thirds of manufactured housing residents are satisfied with their homes and are likely to recommend living in a manufactured home to others.

As the nation continues to navigate an affordable housing shortage exacerbated by the Coronavirus crisis, ensuring that the enterprises support the availability of financing for manufactured homes has never been more important. As manufactured housing, we know all too well the consequences of a lack of federal support for financing for manufactured housing, for affordable housing.

As the enterprises increasingly act more like private entities, eventually operating outside of the supervision of FHFA as conservator, MHI believe it is more important than ever that statutory responsibilities in the form of duty to serve and housing goals are adhered to, and that FHFA holds the enterprises accountable for their compliance with these responsibilities.

MHI appreciates that the Coronavirus crisis has resulted in increased levels of defaults and loan losses for the enterprises. And we understand the enterprises and FHFA are struggling to address this impact through the imposition of repricing of certain types of risks.

But we think that due to the uncertain economic climate that the Coronavirus crisis has created, and with private sector lenders generally being more cautious, this makes the enterprises' role and access to mortgage credit all the more important. And since manufactured housing is the most affordable source of single-family home ownership in America, MHI believes that it is critically important that the enterprises press forward on their duty to serve plans with respect to manufactured housing. And that the FHFA hold the enterprises strictly accountable for their performance relative to the promises made in their duty to serve plans.

The statute requires Fannie Mae and Freddie Mac through duty to serve, to serve three underserved markets, including manufactured housing, in order to increase the liquidity of mortgage investments in those areas and facilitate access to mortgage credit. With respect to manufactured housing, the statute and rule require the enterprises to consider personal property manufactured loans, also called chattel, as well as real estate manufactured home loans. MHI believes access to credit and statutory duty to serve manufactured housing responsibility should remain, if not become more of, a priority for the enterprises.

With respect to personal property loans, the vast majority of manufactured homes are financed as such, 77% of homes that are manufactured are financed where the mortgage is only on the home and not on the underlying land. There is effectively no secondary market currently for these personal property loans. The enterprises have not purchased any personal property loans since some 14 years ago and the volume of FHA Title I personal property loans is minuscule and falling.

There were only 526 FHA Title I loans in 2018 and then only 204 loans in 2019. This makes it all the more critical that the enterprise has followed through on their promises to begin the purchase of personal property manufactured housing loans as laid out in their duty to serve plans. To date, almost two thirds of the way through the second of these two years of the plans, MHI is not aware of any chattel loans that Fannie Mae or Freddie Mac has purchased nor have they participated in a debt structure or guaranteed any loans as stated in their plans.

We strongly urge FHFA to support and hold both enterprises fully accountable for their performance in terms of personal property loan purchase targets in 2019 and 2020. We also urge FHFA to ensure the enterprises in the upcoming planning year continue to take steps to improve their performance on these loans.

As a part of their duty to serve requirements, the enterprises must provide leadership in developing loan products and flexible underwriting guidelines for manufactured home loans, and to increase liquidity and capital available for such loans. This is not just for personal property loans, but also for real property loans.

Under this requirement, MHI believes Fannie and Freddie should continue enhancing the number and flexibility of real property manufactured home loan purchases. Both GSEs have made progress here. They have introduced new programs that provide affordable conventional financing for manufactured homes with site-built features.

As Director Calabria and his team witnessed on the National Mall during HUD's innovative housing showcase, the industry is producing quality homes that are indistinguishable from site-built housing at a fraction of the cost due to the efficiencies of offsite home construction.

One of the homes displayed on the National Mall is a part of the launch of a complimentary class of manufactured home, which MHI is calling cross mod homes. Amenities and features for these cross mod homes include elevated roof pitches, garages and carports, permanent and lower profile foundations and porches and energy efficiencies.

The enterprises support for cross mod homes could not come at a more important time. Particularly as the nation responds to the impact of the pandemic, there has emerged a large group of aspiring homeowners who are currently priced out of traditional site-built housing. These are the consumers that cross mod homes will serve. A robust secondary market with standard mortgage offerings is a critical component of this solution. As the economy continues to recover from COVID, this viable common sense solution to creating more affordable housing needs even more support.

MHI appreciates that both Fannie Mae and Freddie Mac have taken action to launch these programs. However, there are steps that they can each take in the future to make these programs more accessible. And we hope that FHFA will support these efforts, including streamlining the programs and expanding outreach to lenders and appraisers to familiarize them with the programs. These are precisely the type…

Operator: You have two minutes left.

Leslie: Thank you. These are precisely the types of actions that the statute identifies as duty to serve responsibilities. We appreciate the enterprises' work so far and look forward to additional steps being taken to ensure that the innovations of manufactured housing help more Americans achieve quality home ownership at an affordable price.

In conclusion, as you work to establish risk-based capital requirements for the enterprises, we urge you to also be mindful of the need for our nation's secondary mortgage market to support financing for both personal and real property and home loans. MHI fully appreciates the importance of the safety and soundness of the enterprises and we share your interest in ensuring they are well positioned to serve the American homebuyer well into the future.

Today's listening session is important, however, and we appreciate your interest in our views. It is critical that the ultimate decision about capital requirements for safety and soundness do not inadvertently impact the important role the enterprises have to provide affordable and accessible credit to the housing market.

We urge you to find the appropriate balance, and today's listening session indicates your interest in finding that balance, so thank you. We urge you to continue to hold the enterprises accountable for meeting their duty to serve targets. We know this can be

done while balancing safety and soundness concerns with the market and we look forward to further engaging with you as you increase support for manufactured housing.

Manufactured housing is critical to increasing the availability of affordable home ownership. Further involvement by the enterprises in this market will not only strengthen homeownership opportunities, but also offer an alternative to consumers who are hurt by unaffordable rents or the shortage of adequate housing. Thank you again for the opportunity to speak today, this concludes my remarks.

Operator: Thank you, Leslie. Next up is Kristy Fercho. Can you press pound two on your telephone, please? Thank you very much, Miss Fercho. Please go ahead.

Kristy: Great. This is Kristy Fercho on behalf of the Mortgage Bankers Association. First of all, thank you so much for allowing the opportunity to speak on this important issue. As it relates to affordable housing access, the MBA is very committed to promoting greater access to sustainable affordable housing in both single family and multifamily markets. MBA's affordable housing initiative, for example, harnesses the expertise of our membership to forge stronger and more effective affordable housing partnerships in both the policy and business arena.

The GSEs play a crucial role in facilitating access to affordable housing. This role is inherent in their charters, which requires them to promote access to mortgage credit throughout the nation. The MBA fears that the Proposed Capital Rule on balance would decrease rather than increase incentives for the GSEs to promote affordable housing access.

MBA appreciates some of the steps proposed by FHFA to level the capital cost across the GSEs portfolio. The MBA also appreciates the revisions to the problematic features of the earlier proposal that would have penalized small balance loans. Despite these positive elements of the proposal, the aggregate level of capital that would be required is likely to result in increased G-fees, and as a result, increased borrower costs.

Indeed, the GSEs have forecasted G-fees increases of 15 to 35 basis points if the proposal were to be finalized without further charges. If this were to occur, many borrowers would be better off with an FHFA loan rather than a conventional loan, which increases taxpayer exposure to risk and limits options for first time homebuyers.

This aggregate level of required capital can be reduced without jeopardizing safety and soundness by providing more appropriate capital relief for credit risk transfers, reducing the leverage ratio if it is found to be a binding capital constraint too frequently, as is likely the case. And three, making tailored adjustments to risk floors that are duplicative of the leverage ratio.

More broadly, FHFA should clarify its expectations for the GSEs in terms of their supportive affordable housing access prior to the GSEs exiting conservatorship. As with many other elements of the GSEs operations, it is crucial for all stakeholders,

consumers, lenders, servicers, investors, and others, to have a clear understanding of how the GSEs will function post conservatorship. That concludes my remarks. Thank you again for the opportunity to address the committee.

Operator: Thank you very much. Up next is Garth Reman. Please go ahead.

Garth: Good morning. Thank you for opening a new public comment period on the Proposed Capital Rule and holding this listening session to obtain more feedback on its impact on affordable housing access. The National Council of State Housing Agencies is pleased to have this opportunity to deliver these remarks to FHFA on behalf of the state HFAs it represents.

As the next slide says states, state HFAs are the centers of the affordable housing delivering systems in their states. States created HFAs to provide affordable mortgage financing for homebuyers and affordable multifamily project sponsors. HFAs generally serve borrowers most other Fannie Mae and Freddie Mac partners do not.

The next slide shows that HFA homebuyers are typically lower income than first time homebuyers and all homebuyers taken together.

On the next slide, you can see that the median income of renters in HFA-financed housing credit properties on the left side there, are significantly lower than that of all renters.

The next slide shows that HFAs had served higher percentages of people of color than other lenders in many of the last 18 years with some states devoting more than half their recent lending activity to minorities. Next slide, please.

The enterprises programs and activities have provided significant benefits to state HFAs by enabling the HFAs to increase their affordable home ownership lending. In turn, the enterprises have benefited by obtaining more high quality, affordable goals rich loans than they likely otherwise would have. These loans help the enterprises meet their charter mandates to support affordable housing and underserved markets.

At the end of 2019, state HFA portfolios held more than $26 billion of enterprise mortgage products. The next slide shows how the HFA's impact, supported in large part by the enterprises, has grown substantially over the last ten years.

As the next slide shows, HFA lending is safe and sound, with the lower red line in the graph showing Fannie Mae HFA loans have lower default rates than Fannie Mae loans to non-HFA but similar borrowers. Next slide, please.

The proposed capital standards have serious flaws that will jeopardize Fannie Mae's and Freddie Mac's ability to meet their vital affordable housing missions. By overstating the risk of some loans and increasing capital requirements for them, the standards would require the enterprises to hold more capital than necessary to accurately reflect these loans' risk. This will reduce the enterprises efficiency and drive them away from mostly

safe and sound affordable housing business. Holding too much capital poses problems as well as holding too little does.

I also want to note that the proposed capital standards, even if applied only after the GSEs leave conservatorship, produce a strong and tangible effect on the enterprises' current business. In crafting the proposed capital standards, FHFA says it was driven by the enterprises' statutory mission to provide stability and ongoing assistance to the secondary mortgage market across the economic cycle. While this is an important part of the GSEs public purpose, it is not all of it. Next slide, please.

FHFA's framework does not consider the rest of the GSE's public purpose. Namely, to support activities relating to mortgages on housing for low and moderate income families involving a reasonable economic return that may be less than the return earned on other activities, and to help foster access to credit and underserved markets. The standards will particularly disadvantage affordable housing loans that incorporate one or more of many of the risk multipliers identified in the framework.

Some of these borrower or loan characteristics that would require upward risk adjustments include higher original loan to value ratios, lower FICO scores and subordinate financing in the form of down payment assistance, which is so necessary for many credit worthy borrowers.

Our concern is that the framework ignores the ways HFAs and others constructured loan terms and down payment assistance to reduce risk rather than increase it. The standards would also require higher capital charges and hence, G-fees and rate than necessary on many affordable multifamily loans.

The framework would do this because it fails to recognize the risk-reducing impact of some factors common to many affordable multifamily transactions, including additional subsidies, low income housing tax credit financing, tax abatements, and supportive services.

As the next slide says, NCHA urges FHFA to rethink the proposed capital framework and establish new standards that consider not only the enterprises' obligation to avoid losses and facilitate liquidity, but also their mandate to support affordable financing for single family and multifamily housing. FHFA should modify the capital standards to enable the enterprises to meet their affordable housing mission by exempting state FHFA loans from some or all of the higher capital requirements, especially those loans with down payment assistance structured in ways that mitigate default risk.

As it says on the next slide, we also recommend that FHA eliminate the proposed risk adjustment for loans that allow borrowers to remove mortgage insurance after their loan to value ratios drop below levels, widely considered to minimize default risk.

Additionally, FHFA should eliminate or decrease risk adjusters for buyers who demonstrate faithful payment history through non-mortgage installment payments, remove the risk multiplier for sound condominium lending, minimize penalties and

introduce flexibilities for home repair lending, and differentiate between different kinds of third party lending management and oversight.

Specifically relating to multifamily mortgage exposures, NCHA urges FHFA to lower the risk adjustments for affordable rental properties that use additional subsidies, supplemental tenants services, housing credit, and tax exempt bond financing, property tax abatement, energy retrofits, or income diversification, and other risk mitigating measures. The next slide adds that we urge FHFA --

Operator: Sorry to interrupt but there's about two minutes left.

Garth: Thank you. To re-examine the risk waiting for small multifamily loans, to more accurately reflect the risks posed by many affordable small multifamily properties, including many of the factors I have just mentioned that we discussed in our written statement.

A recurring factor we notice in the standards is the overly broad and generalized manner in which the standards apply to groups of loans that are likely to have significantly different risk characteristics.

Therefore, and finally, FHFA should make its final framework flexible enough to adapt to an evolving market where new ideas are likely to emerge. The development of these new ideas should be valued and encouraged by state HFAs mortgage lenders, the enterprises, and FHFA. We hope that FHFA will ensure that the capital framework does not pose an obstacle to that pursuit.

Thank you for the opportunity to reinforce our written comments today. In conclusion, as are my last slide says, with the changes we recommend we are confident FHFA can develop a capital framework that will protect the enterprises, keep them on a path out of conservatorship and enable them to meet their vital affordable housing mission. If FHFA doesn't make these changes, we are concerned the capital framework will fall short in reaching any or all of these goals. Thank you very much. That concludes my remarks.

Operator: Thank you. Next up is Edward Pinto. Please go ahead.

Edward: Thank you. And thank you for the opportunity to present on this crucial topic. Next slide, please. I would like to cover three components of US housing policy that disproportionately impact low income households and limit access by unsustainably boosting home prices.

Price booster number one, supply constraints in the form of overly restrictive zoning and other land use restrictions. These drive up the cost of land and new construction, create artificial scarcity of land that's driving up home prices, both new and existing.

Price booster number two, risky, highly leveraged federally guaranteed home loans which increased demand against the limited supply. The enterprises encounter or

engage in unseemly and dangerous taxpayer funded competition with HFA over high risk loans made to low income homebuyers. This permits one homebuyer to bid up against another for scarce goods, namely homes. Leverage enhancing tools quickly get capitalized into higher prices and increased risk.

Price booster number three, historically low interest rates which are largely the result of monetary policy can also get quickly capitalized. Next slide, please.

Many low-income homeowners are pushed into a vicious cycle of price volatility, limited wealth building and high default rates. This is best demonstrated by thinking about how house prices actually work. In 2012, a home in Phoenix might have sold for $100,000. Today, that home might sell for $200,000. It's the same home. In 2012, the structure portion of that home might have been $80,000 and the land portion $20,000. Today the structure portion might be $100,000 and the land portion $100,000.

That means that the property doubled, the structure value went up by 25%, but the land price or value went up by five times or 500%. So the land ratio is not 20% where it started by 50%. Nothing strips wealth faster from low income buyer -- homeowners than being sandwiched between high LTVs and high DTIs, which really defines HFA lending and many of the enterprises' affordable housing loan. This fuels unknowing land speculation by homeowners with minimal resources to fall back on during the negative feedback loop of declining prices and incomes. Next slide, please.

The most important indicator of land speculation and home price volatility is the rapid rise in land prices unsupported by an increase in utility. High risk subsidized mortgage credit tends to push up the price of land, this makes homes less, not more affordable. These affects are widespread and notable and are an unintended effect of FHFA insurance and the enterprises' affordable lending programs and the enterprises' weak capital regime.

Low income households are harmed due to increased foreclosure risk, limited wealth building and reduced home buying opportunities. This is a fair housing violation for households of color as these federal policies have a disparate impact on them. Next slide, please.

The rate of home price appreciation is directly correlated to leverage as measured by mortgage risk index. Low price tier, one of the entry level price tiers that represents the price point at 40% of FHA sales prices. the low-price tier has the highest mortgage risk index and the highest house price appreciation.

This chart shows for Phoenix, similar charts are available for dozens and dozens of other metros. In the case of Phoenix, house prices started out with at an index of 100. Low priced homes started out at 100, went to about 250% or an increase of 150% in the price. High priced homes, however, went up only 55%. So this is due to the very high level of risk on these loans, which you'll see in this subsequent slide. Next slide, please.

Taxpayer backed default prone loans, boost demand, which fuels house price appreciation in excess of inflation and translates into unsustainable increases in land share. Stressed mortgage default rates are highest, the orange circles on this slide, among lower priced homes. See the X axis is home price again in Phoenix, ranging from around $200,000 at the low end up to about $800,000 at the high end.

On the X axis, the change in land share, as I indicated earlier, it's this excess house price appreciation that gets translated into excess land share increases. And as a result, the low-priced homes have the highest change in land shares, that share of the home's value. This is because leverage is capitalized into higher land prices. Next slide, please.

In this slide, the stressed mortgage default rate which is on the Y axis is an important indicator of speculation and potential for future foreclosures in home price declines. The X axis shows recent change in land value. Note that the X axis starts at around 100%, which means that land values double and goes up to 800, 900 or even a well over a thousand percent. The circles are color coded based on minority share.

And you'll note that the minority, the higher minority shares those above about 45% at a zip code level, are disparately impacted by this policy. They're the ones that have the massive increases or most massive increase in land prices. It's largely due to the combination of leverage and the scarcity of supply. Next slide, please.

Nothing strips home equity faster from low income homeowners than unknowing land speculation. Here the Y axis showed what happened last time. All the numbers here are negative because, they're showing the decline in land share after the peak that occurred in Phoenix in 2006 and 2007. Land prices then collapsed until they hit bottom around the beginning of 2012. And so the change in land -- in house prices got translated to much larger changes in reduction in land share. And you see that in some cases, the land share went down by 70%.

The X axis here shows the recent change in land share that's occurred during the boom that started in 2012 and continues and has accelerated through today. And you see that the same zip codes that were hurt the most last time are being hurt again, this time. The size of the circle represents the income quintile of the homeowners and the minority share is the orange, represented by the orange and blue color. And you see the large concentration of orange that occurred last time with a massive decline in land share and it potentially will occur this time with a massive increase in land share. It also correlates very highly to income. Next slide, please.

This next slide shows how this translates into collateral risk for those homeowners who were speculating in land depreciation. The upper left quadrant is a combination of very high change in land share, the X axis, and very high change in terms of the, or excuse me, very high level of mortgage risk index, the Y axis. And if you have both of those things, you're in the high mortgage risk category and the high house price appreciation translating to the land share category.

The low, low is in the lower last. And gain, we see that income quintiles as evidenced by the orange, the bottom two quintiles, bottom 40% of the homebuyers in these cases in Phoenix, are concentrated almost entirely in the high, high category. Next slide, please.

We see the same thing this time for minority share and we see that the minority share is concentrated even more highly and at a higher level in terms of mortgage risks than for lower income because the minorities are even more disparately impacted by these policies. Next slide, please.

For solutions to increase housing access there's no taxpayer costs. One, Fannie and Freddie's unseemly and dangerous taxpayer funded competition with FHA over high risk loans to low income buyers. Two, adopt strong enterprise capital and counter cyclical policies as suggested in our comment letter. Three, relieve supply constraints with light touch density, which is to change the status quo to allow two, three, and four unit homes to supplement housing stock in one family residential neighborhood. And four, reduced FHA and GSE lending by converting to wealth building home loan.

Home ownership can be an effective way to build wealth, but only if homeowners buy a house they can comfortably afford to minimize risk of default, restrict the tapping of equity to improving the house, not supporting lifestyle expenditures, pay off the mortgage well before retirement. The wealth putting home loan is designed to meet precisely those goals. Thank you again for the opportunity to make this presentation.

Operator: Thank you very much. Would Gerron Levi, please press pound two on your phone? Thank you, please. Go ahead.

Gerron: Good morning. Thank you for this opportunity to provide additional views on the Re-proposed capital standards. We realize a capital framework is an essential step in the enterprises being released from their long-standing conservatorship. We have supported their release. However, we are very concerned about the bank-like capital requirements being proposed for the GSEs, the impact it would have on their role in the larger housing finance system and on the access and affordability of mortgage credit for low and moderate income and minority borrowers and in underserved market, if the framework is not significantly modified.

The National Community Reinvestment Coalition and its grassroot member organizations are actively engaged in the conversation around access to home ownership and the wealth building opportunity it can create. We are also committed to protecting and strengthening the formative -- the affirmative obligations or so-called duties to serve throughout the housing finance system, which play a critical role in providing access to mortgage credit for LMI and minority borrowers and in traditionally underserved markets.

Fannie and Freddie have an affirmative obligation to facilitate the financing of affordable housing for LMI families in a manner consistent with their overall public purposes, while maintaining strong financial conditions and reasonable economic return.

In our advocacy, we have consistently urged FHFA to set strong enterprise housing goals and rigorous standards for their statutory duty to serve underserved markets, consistent with the affordable housing mission. We have also urged that they improve the distribution of loan guarantees across the credit score spectrum, as well as their guarantees into some segments of the markets, such as for African American homebuyers.

Pursuant to their affordable housing and fair lending obligations, Fannie and Freddie's role not only includes the purchase of mortgages. They have a significant number of staff researching the market and developing affordable housing products to fill gaps in market access, conducting outreach in underserved markets and with stakeholders serving minority borrowers. Doing grant making and making other strategic investments.

As noted by one enterprise, the GSEs together provide approximately 40% of loans targeted to low and very low-income borrowers supporting both public and private programs. The Re-proposed Capital Rule is quite consequential. And we are very concerned about aspects of the Proposed Rule that would make the enterprises less able to support their affordable housing mission.

As we expressed in our earlier -- in an earlier comment letter with others, we do believe the public comment period could have been greatly enhanced by better information from the agency about the real-world impacts of the Proposed Capital Rule. Nonetheless, NCRC joined with a number of our affordable housing and civil rights allies in raising concerns about the over capitalization of the GFEs that the Proposed Rule represents. And about the disproportionate impact it would have on LMI and minority borrowers and in underserved markets.

Among other recommendations, collectively we have urged the agencies to reject bank-like capital standards for the GSEs and to adopt capital standards more appropriately to the monoline secondary market mortgage companies that they are. The counter portion of their guaranteed fee revenue as capital for risk-based capital requirements, and to eliminate the punitive stability capital buffer and the counter cyclical capital buffer.

While Fannie Mae and Freddie Mac's public comments came late in the comment process, they magnified some notable concerns about the impact of some aspects of the Proposed Capital Rule, and how they would affect affordable housing. While we appreciate FHFA’s effort in the Proposed Rule to provide more level application of capital requirements across risk levels, the minimum capital requirements on low risk loans are too high. And when combined with other features of the proposal, like a high binding leverage ratio, they would reduce the amount of cross subsidization the GSEs can use to expand access to mortgage credit.

The GSEs’ comment letters, for example, raise a number of concerns. Freddie Mac notes that an increase of 20 to 50 basis points could be required on the higher risk segments of their acquisitions to offset the loss of higher returns and volume on their lower risk segments, affecting low income affordable housing.

While Fannie acknowledges some unpredictability in the level of guaranteed fee increases that would occur, noting that it would depend on factors such as market returns expectations, credit characteristics of acquired loans, the amount of capital that management deemed necessary to hold above the regulatory minimums, competitor pricing strategies and mortgage market conditions.

However, in the two potential scenarios they lay out, they note that the effect may fall on borrowers least able to afford the fee increases. Freddie also notes that the proposed refinance burnout multiplier would apply a high proportion -- would apply to a high proportion of lower balance affordable loans, which have a lower propensity to prepay than other loans in their portfolio.

Increasing required capital for these loans may cause pricing for them also to increase. As the agency knows, this is a segment of the market that already has significant access challenges.

On the issue of low balance loans, our joint comment urges the agencies to keep improvements over the 2018 proposal by removing the surcharges for low balance loans, as well as single borrower loans.

On another issue, Fannie also indicates that eliminating the risk multiplier for multifamily mortgage exposures with a government subsidy, such as Y-tech and Section Eight, would make it more expensive to provide liquidity for property serving the neediest tenants and potentially reduce funding for property maintenance and tenant care. It could all result in fewer transactions that are feasible economically, potentially increasing the existing supply gap for affordable rental housing.

We urge the FHFA to address these concerns and those raised in our joint comment letter and importantly, to keep the enterprises' affordable housing mission, as well as their related statutory and fair lending obligations front and center as you finalize the capital framework. Thank you and that concludes my remarks.

Operator: Thanks very much. Up next, we have Jeffrey Krohn.

Jeff: Hello, this is Jeff Krohn and I lead the Global Mortgage Credit Practice at Guy Carpenter. Guy Carpenter is one of the Marsh & McLennan businesses, and we work in the capacity of a reinsurance intermediary to transfer credit risk from the enterprises, as well as from mortgage insurers to well-rated global reinsurers.

First, we want to commend the FHFA for doing the job it is doing in the wake of COVID-19 to help borrowers and renters who are at risk of losing their home due to the Coronavirus national emergency. Your work is making a difference in the lives of millions of Americans.

And amidst these -- this challenging backdrop, the FHFA has remained committed to establishing a post conservatorship regulatory capital framework. Guy Carpenter recognizes the immense amount of effort that went into drafting the Capital Rule. Your

proposal though, not perfect, shows thoughtfulness and your process shows an openness to consider other points of view. Guy Carpenter's appreciative to have shared its comments in writing and discuss our perspective on affordability here today.

The path to exiting conservatorship requires sufficient private capital so that the enterprises may be independent and viable participants in the housing market. The enterprises need to attract private capital and lots of it. And on this path to exiting conservatorship, the FHFA must find a way to bridge the chasm between protecting the taxpayer and supporting affordable housing through all economic environments. If the cost of capital is too high and the chasm too wide, it can have material consequences on guarantee fees and harming housing affordability and underserved borrowers.

Today, we will address the impact of increasing guarantee fees and the importance of credit risk transfer in reducing the overall cost of capital to the enterprises.

Increasing guaranteed fees are inevitable to exit in conservatorship, and it will have two effects as we see it. First, increases in guarantee fees will flow through to those borrowers with enterprise backed loans, making them more expensive. But reduced affordability is a fairly obvious outcome. The less obvious outcome is increased guarantee fees could create adverse selection within the enterprises' portfolios.

The topic of adverse selection has long been the subject of insurance in business school case studies. In the case of the enterprises, increased guarantee fees will cause adverse selection with the highest quality borrowers. Those with the high FICO scores, large down payments and strong stable incomes.

Unsurprisingly, these borrowers have their choice of options when obtaining a mortgage. So if the enterprises increase guarantee fee is too much, the highest quality borrowers will find a more economic outlet elsewhere. The loss of these low risk guarantee fees will indirectly create affordability issues, because the most attractive borrowers are critical for funding the higher risk, underserved segment of the market, which today is cross subsidized by these low risk loans.

Not having balance from high credit quality borrowers will increase credit risk within the enterprises and reduce affordability. Therefore, it is imperative to mitigate the increase to guarantee fees as much as possible.

Having a thoughtful capital framework that allows the enterprises to efficiently manage their cost of capital is paramount to limiting increased guarantee fees. If the enterprises can reduce their cost to capital, they mitigate increases to guarantee fees and improve affordability.

The Proposed Rule highlights the superior quality of equity capital. We would generally agree with this concept. After all, equity responds to all the risks to which the enterprises are exposed. Operational risk, to which CRT does not respond, market risk, again to which CRT does not respond, and to credit risk, to which CRT does respond. But

credit risk also comprises 86% of the risk held by the enterprises as the Proposed Rule notes.

While high quality equity capital responds to all forms of risk, it also comes with the highest cost of capital. Most equity investors demand 10% to 15% returns for their capital. There's no doubt that supporting the enterprises' capital stack with equity capital would result in the highest possible increase to guarantee fees.

But if the enterprises can access other forms of high quality capital, but come with lower cost, affordability outcomes will improve. Depending on proximity to risks, CRT capital is less expensive than equity capital. Let's examine three reasons why that is.

Credit risk capital does not respond to all forms of risk, just credit risk. And that's okay since CRT responds to the dominant risk in the enterprises' portfolio credit risk. So as long as there is foundational equity capital, CRT can reduce the overall cost of capital by better aligning capital to risk. It's instructive to look at other examples of risk-bearing entities that have massive concentrations of a dominant risk and how they align capital to risk.

Take the example of dozens of property insurance companies that operate in the state of Florida. The dominant source of risk to which they expose their balance sheets is hurricanes. None of these companies are entirely capitalized by equity capital. That would be prohibitively expensive and make them uncompetitive.

Instead, they all have substantial catastrophe reinsurance programs that form a portion of their capital stack and transfer risk to well capitalized reinsurers and investors. This remote and catastrophic risk is better aligned with highly specialized investors and reinsurers that specialize in catastrophic property risk. We believe the same is true with matching lower costs, CRT capital, to remote credit risk.

Secondly, accessing competitive diverse pools of private capital results in lower costs of capital. Reinsurers and fixed income investors that participate in CRT target stable, predictable returns on credit investments rather than more volatile, higher upside returns that equity investors seek.

Fixed income investors and reinsurers have highly specialized teams that focus solely on credit risk, enabling them to model and price credit risk efficiently. CRT provides an avenue for these credit risk investors to deploy considerable amounts of capital to the enterprises that would not otherwise entertain an equity capital investment. CRT makes equity capital more attractive by increasing certainty of income, absorbing losses, and reducing volatility.

Operator: Sorry to interrupt. You have two minutes left.

Jeff: Perfect, thank you. The business model of the enterprises has to evolve. CRT capital enhances the ability of the enterprises to emerge from conservatorship by reducing the overall cost of capital and cost to the US homeowner. Embracing CRT embraces

affordability. We wish you luck as you finalize and properly calibrate the capital framework that appropriately recognizes the benefits of CRT and positions the enterprises to exit conservatorship and bridge the important gap between affordability and protecting the US taxpayer.

Guy Carpenter remains committed to engaging in productive discussion and solution seeking on this extremely important topic for our country and economy. Thank you for your time this morning.

Operator: Thank you. And our final speaker is Elizabeth Laberge.

Elizabeth: Good morning. My name is Elizabeth Laberge and I'm Senior Regulatory Council with the National Association of Federally Insured Credit Unions, or NAFCU. NAFCU advocates for all federally insured not for profit credit unions, which in turn serve 121 million consumers with personal and small business financial service products. NAFCU appreciated the opportunity to provide feedback on the FHFA's re-proposal of its regulatory capital framework. And we're also grateful that you've established this listening session to continue to obtain additional feedback on the re-proposal's potential impact on affordable housing.

The capital reserve requirements that result from the re-proposal are higher than necessary. And as drafted, the re proposal would likely establish capital levels that exceed the worst-case loss scenario developed by the Federal Reserve. The potential harms of setting capital levels too high are significant for credit unions and their members.

As member owned, not for profit cooperatives, credit union to have a long history of offering products and services to low income, moderate income and underserved individuals. Increases in the cost of credit in the form of increased guaranteed fees and mortgage rates would have a significant negative impact on credit unions' ability to serve these less wealthy members.

If finalized as written, the capital framework could result in an increase of mortgage rates between 15 and 25 basis points. And this increase in the cost of credit could impact communities most in need of access to credit and affordable housing.

Pushing these consumers out of the access to home ownership unnecessarily would be completely at odds with the GSEs obligations to serve low income, moderate income, and underserved families, and to support affordable housing preservation under the Federal Housing Enterprises Financial Safety and Soundness Act, and the Housing Economic Recovery act of 2008. More can and should be done to ensure access to housing finance for these borrowers.

NAFCU appreciates the FHFA's recent efforts to incorporate alternative credit scores, because this can provide critical benefits to low- and moderate-income borrowers who may have no or low FICO scores. But FHFA must ensure that appropriate cross subsidies and low- and moderate-income borrowers remain in place and are not distorted by

capital requirements. Pricing of credit risk based cross subsidies should reflect the actual credit risk posed by the loan and not simply third classic FICO scores.

We also urge the FHFA to consider an adjustment of the base risk weights for mortgages originated by credit unions and other categories of originators that make mortgage loans that are statistically lower risk and serve low income, moderate income, and underserved borrowers at a higher statistical rate than mega banks and other lenders.

If the FHFA has performed its own analysis on the potential increase to the cost of credit as a result of the re-proposal, it has not shared that analysis with the public. And their responses to the re- proposal, both Fannie Mae and Freddie Mac confirmed that these will have to increase to meet these high capital requirements. And these high increased costs will result in higher rates for borrowers.

We would ask that the FHFA they conduct a thorough analysis of these outcomes and their effect on affordable housing before finalizing the rule. The data and the results of that analysis should be included in the preamble to any final rule or a supplemental document to provide transparency to the mortgage servicing industry and to borrowers.

We appreciate the opportunity to share the perspective of our member credit unions, and that is the conclusion of my remarks.

Operator: Thanks everyone. Do we have closing remarks?

Naa Awaa: This concludes the session. Yes, thank you.

Operator: Thank you. That concludes our conference. Thank you for using Events Services. You may now disconnect.