

# Don't Blame the Affordable Housing Goals for the Financial Crisis

## Federal Research

### 1. [Financial Crisis Inquiry Report \(2010\)](#)<sup>1</sup>

*"Conclusions of the Financial Crisis Inquiry Commission"*

"We also studied at length how the Department of Housing and Urban Development's (HUD's) affordable housing goals for the GSEs affected their investment in risky mortgages. **Based on the evidence and interviews with dozens of individuals involved in this subject area, we determined these goals only contributed marginally to Fannie's and Freddie's participation in those mortgages.**"

"Using data provided by Fannie Mae and Freddie Mac, the FCIC examined how single-family, multifamily, and securities purchases contributed to meeting the affordable housing goals. In 2003 and 2004, Fannie Mae's single- and multifamily purchases alone met each of the goals; in other words, the enterprise would have met its obligations without buying subprime or Alt-A mortgage-backed securities. **In fact, none of Fannie Mae's 2004 purchases of subprime or Alt-A securities were ever submitted to HUD to be counted toward the goals.**"

"Yet all but two of the dozens of current and former Fannie Mae employees and regulators interviewed on the subject told the FCIC that **reaching the goals was not the primary driver of the GSEs' purchases of riskier mortgages and of subprime and Alt-A non-GSE mortgage-backed securities.** Executives from Fannie, including Mudd, pointed to a "mix" of reasons for the purchases, such as reversing the declines in market share, responding to originators' demands, and responding to shareholder demands to increase market share and profits, in addition to fulfilling the mission of meeting affordable housing goals and providing liquidity to the market."

"Former OFHEO Director Armando Falcon Jr. testified that **the GSEs invested in subprime and Alt-A mortgages in order to increase profits and regain market share and that any impact on meeting affordable housing goals was simply a by-product of this activity.**"

2. [Federal Reserve Bank of St. Louis \(2014\)](#)<sup>2</sup>

*"Did Affordable Housing Legislation Contribute to the Subprime Securities Boom?"*

"In this paper we examined the effect of affordable housing legislation on the volume, pricing, and performance of securitized subprime mortgages originated in California and Florida in 2004 through 2006. Using a regression discontinuity approach, **we find no evidence that the affordable housing goals of the CRA or of the GSEs affected any of these outcome measures.** This finding is robust to the inclusion of various, to the sample of only full documentation loans, and to different bandwidths for the regression discontinuity specification. We also find that the majority of mortgages packaged into subprime MBS went to borrowers with high stated income: Average borrower income for such mortgages was about \$100,000. While we provide evidence that Fannie Mae and Freddie Mac held substantial amounts of subprime PLMBS, and that their holdings of these securities played a significant role in their demise, the evidence in this paper refutes the claim that the affordable housing mandates were responsible for the subprime crisis. We hope our findings stimulate researchers to seek other explanations for the subprime securities boom."

3. [Divisions of Research & Statistics and Monetary Affairs Federal Reserve Board \(2012\)](#)<sup>3</sup>

*"The Government-Sponsored Enterprises and the Mortgage Crisis: The Role of the Affordable Housing Goals"* March, 22, 2012

"Since the UAG (Underserved Area Goals) had such a small effect on GSE purchases in poor and underserved areas at the peak of the subprime mortgage market, **I conclude that the goal and the GSEs' purchases of single-family whole loans in these areas were not the drivers of the subprime market.** Thinking about the UAG as a proxy for the AHGs as a whole, as is custom in the literature, **I posit that single-family mortgage purchases made by the GSEs in response to the goals were not responsible for driving the increase in the number of high-risk borrowers in the mortgage market prior to the crisis.**"

## Academic Research

4. [Dwight M. Jaffee- Haas School of Business, University of California, Berkeley](#) (2010)<sup>4</sup>

*The Role of the GSEs and Housing Policy in the Financial Crisis (Presented to the Financial Crisis Inquiry Commission)*

**"I do not consider the GSE housing goals for lending to lower-income households and in lower-income regions to have been a primary factor motivating the GSE investments in high-risk mortgages.** However, I recommend further research to determine which GSE high-risk mortgage features created the highest default propensities, and whether these features are also a common component of the GSEs' housing-goals-eligible mortgages."

5. [Ellen Harnick- Western New England Law Review \(2009\)](#)<sup>5</sup>

*The Crisis in Housing and Housing Finance: What Caused It-What Didn't-What's Next*

**“These claims are similarly unsustainable.** While Fannie Mae and Freddie Mac should be strongly criticized for purchasing subprime mortgage-backed securities, their role in purchasing and securitizing problem loans was small in comparison to that of private industry. **All subprime mortgage-backed securities were created by Wall Street. Fannie Mae and Freddie Mac did not securitize any of these loans because the loans did not meet their standards.”**

**“Nor can it be claimed that pressure to meet affordable housing goals drove the entities to invest in Alt-A mortgages.** Because of the income characteristics of Alt-A borrowers, the entities’ investment in these loans would have actually diluted their affordable housing ratios. Other pressures-to boost shareholder returns and keep up with industry-drove the decision.

6. [Robert B. Avery and Kenneth P. Brevoort-Review of Economics and Statistics \(2015\)](#)<sup>6</sup>

*The Subprime Crisis: Is Government Housing Policy to Blame?*

“Some have suggested that housing policy, embodied by the Community Reinvestment Act (CRA) and **affordable housing goals of the government-sponsored enterprises (GSEs)**, caused the subprime crisis. We examine if these programs led to worse mortgage outcomes using two approaches. The first examines whether more activity by CRA-covered lenders, or more loan sales to the GSEs, was associated with worse outcomes. The second uses regression discontinuity to determine if outcomes were worse at the geographic thresholds used by each program. **Our results suggest that neither program played a significant role in the subprime crisis.”**

7. [Shawn Moulton- Journal of Housing Economics \(2014\)](#)<sup>7</sup>

*Did affordable housing mandates cause the subprime mortgage crisis?*

“The 1992 Federal Housing Enterprises Financial Safety and Soundness Act (GSE Act) mandated that a specified percentage of Fannie Mae and Freddie Mac purchases come from underserved populations. A number of prominent observers have pointed to the GSE Act as a root cause of the recent housing crisis. This paper evaluates the link between the GSE Act and relaxed mortgage market standards. Using loan application-level data from the Home Mortgage Disclosure Act, I analyze whether the GSE Act’s single-family affordable housing goals altered mortgage lending or purchasing decisions. To identify this effect, I use a regression discontinuity design that exploits arbitrary cutoffs used to

determine whether a loan satisfies the GSE Act goals. **I find that the GSE Act's single-family affordable housing goals increased GSE purchases from very low-income borrowers by 4.4% but had no effect on mortgage lending.** These results stand up to a number of specification and robustness checks."

8. [Valentin Bolotnyy- Real Estate Economics \(2014\)](#)<sup>8</sup>

*The Government-Sponsored Enterprises and the Mortgage Crisis: The Role of the Affordable Housing Goals*

"I use regression discontinuity analysis to measure the effect of one of the Affordable Housing Goals, the Underserved Areas Goal (UAG), on the number of whole single-family mortgages purchased by Fannie Mae and Freddie Mac (GSEs) in undeserved census tracts for 1996–2002. Focusing additionally on tracts that became UAG-eligible in 2005–2006, I measure the effect of the UAG during peak years for the subprime market. **The results suggest a small UAG effect and challenge the view that the goals caused the GSEs to supply substantially more credit to high-risk borrowers than they otherwise would have supplied during the subprime boom.**"

## Think Tanks and Nonprofit Research

9. [Center for American Progress \(2011\)](#)<sup>9</sup>

*Faulty Conclusions Based on Shoddy Foundations: FCIC Commissioner Peter Wallison and Other Commentators Rely on Flawed Data from Edward Pinto to Misplace the Causes of the 2008 Financial Crisis*

"Pinto also wrongly blames the affordable housing goals of Fannie and Freddie for the origination of Alt-A loans, which under his analysis account for 65% of the "high risk" mortgages attributable to Fannie and Freddie. **In fact, these Alt-A loans (either according to the normal usage of "Alt-A" or Pinto's newly invented definition of "Alt-A") would not have qualified for the affordable housing goals.**"

10. [John C. Weicher \(George W. Bush appointee\) \(2010\)](#)<sup>10</sup>

*The Affordable Housing Goals, Homeownership and Risk: Some Lessons from Past Efforts to Regulate the GSEs*

"It has sometimes been asserted that the affordable housing goals established in 2005 are substantially responsible for the GSEs' collapse in 2008."

"In fact, the GSEs had been buying A-minus and Alt-A loans since the later 1990s, according to analyses during the process leading up to the 2000 rule. **They increased**

**their subprime activity in 2003, before the new goals were proposed for comment in May 2004, and for that matter before Freddie Mac's accounting problems came to light.** There is direct evidence on the extent to which the GSEs were buying subprime mortgages, both before and after the 2005 rule went into effect. **This evidence indicates that the affordable housing goals had little if any impact on GSE activity in these markets. Instead, it appears that the GSEs were responding to the same factors in the mortgage market as other lenders."**

11. [Center for American Progress \(2017\)](#)<sup>11</sup>

*The 2008 Housing Crisis: Don't Blame Federal Housing Programs for Wall Street's Recklessness*

**"It is unlikely that the GSEs' long-standing affordable housing goals encouraged lenders to increase subprime lending.** Since 1992, Fannie Mae and Freddie Mac have been subject to affordable housing goals designed to help target their support of single-family and multifamily mortgages lending in order to increase homeownership in economically marginalized communities. The goals originated in the Housing and Community Development Act of 1992, which passed with overwhelming bipartisan support."

**"Despite the fairly broad mandate of the affordable housing goals, there is little evidence that directing credit toward borrowers from underserved communities caused the housing crisis.** The program did not significantly change broad patterns of mortgage lending in underserved communities, and it functioned quite well for more than a decade before the private market began to heavily market riskier mortgage products."

## Op-eds

12. [John C. Weicher \(George W. Bush appointee\)- National Review \(2010\)](#)<sup>12</sup>

*At the Fall of HUD*

**"The affordable-housing goals are a wonderful excuse.** They let the GSEs off the hook and shift the blame to the Bush Administration, at the same time diverting attention from the refusal of congressional Democrats to allow stronger regulation of Fannie and Freddie after their accounting scandals surfaced in 2003. The goals are even blamed by some conservatives, who see them as credit allocation, and overlook the special privileges conferred on the GSEs by their federal charters which create something close to a federally sponsored duopoly in the mortgage market.

**But this convenient explanation doesn't fit the facts.**

The GSEs began buying subprime mortgage-backed securities (MBS) heavily in 2002. Their purchases of sub-prime MBS doubled between 2002 and 2003, and doubled again in 2004 — from \$38 billion to \$81 billion to \$176 billion. **All this happened before the housing goals were changed in 2005."**

13. [David Sanchez- Think Progress \(2016\)](#) <sup>13</sup>

*No, Lending To Poor People Did Not Cause The Financial Crisis*

- **The argument that CRA and the affordable housing goals caused the crisis have been debunked time and time (and time and time and time) again.** The CRA has been in place since 1977, while subprime lending only skyrocketed in the 2000s. Even if one concentrates on the changes in enforcement of the act in 1995 (as Gramm does), the Act does nothing to explain the massive uptick in subprime lending concentrated from **2004 to 2006**. What's more, most subprime lenders **weren't banks** and therefore weren't even subject to CRA. That's why **only 6 percent** of the high-cost mortgages at the time (a proxy for subprime) could even potentially qualify for CRA credit."

14. [Senator Elizabeth Warren \(D-MA\) -Huffington Post \(2013\)](#) <sup>14</sup>

*Elizabeth Warren Destroys Financial Crisis Myth*

"Although Fannie and Freddie purchased securities backed by subprime loans, and some of those purchases helped fulfill their affordable housing goals, the **St. Louis Fed economists found that the housing goals had no impact — no impact** — on either the number of subprime loans originated or the price of those loans in the private-label market," she said. "Affordable housing goals have been scapegoated by those who have been itching to get rid of the goals for a long time, but I think it's time to drop that red herring."

## Endnotes

- 1 United States. (2010). *The financial crisis inquiry report: Final report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*. Washington, DC: Financial Crisis Inquiry Commission. Retrieved from <https://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf>
- 2 Hernández-Murillo, R., Ghent, A. C., & Owyang, M. T. (2014, December). *Did Affordable Housing Legislation Contribute to the Subprime Securities Boom?* (Federal Reserve Bank of St. Louis, Research Division). Retrieved from <https://research.stlouisfed.org/wp/2012/2012-005.pdf>
- 3 Bolotnyy, V. (2012). *The Government-Sponsored Enterprises and the Mortgage Crisis: The Role of the Affordable Housing Goals* (Board of Governors of the Federal Reserve System, Office of Financial Stability Policy and Research). Retrieved from <https://www.federalreserve.gov/pubs/feds/2012/201225/201225pap.pdf>
- 4 J Financial Crisis Inquiry Commission (2010) Testimony of Dwight M. Jaffee entitled “The Role of the GSEs and Housing Policy in the Financial Crisis”. Retrieved from [http://www.nytimes.com/packages/pdf/jaffee\\_report.pdf](http://www.nytimes.com/packages/pdf/jaffee_report.pdf)
- 5 Harnick, E. (2009) The Crisis in Housing and Housing Finance: What Caused It - What Didn't - What's Next 31 W. New Eng. L. Rev. 625 Retrieved from <http://digitalcommons.law.wne.edu/cgi/viewcontent.cgi?article=1020&context=lawreview>
- 6 Avery & Brevoort (2014), The Subprime Crisis: Is Government Housing, Policy to Blame? The Review of Economics and Statistics 97, 352-363. Retrieved from [https://www.mit-pressjournals.org/doi/abs/10.1162/REST\\_a\\_00491](https://www.mit-pressjournals.org/doi/abs/10.1162/REST_a_00491)
- 7 Shawn Moulton, Did affordable housing mandates cause the subprime mortgage crisis?, In Journal of Housing Economics, Volume 24, 2014, Pages 21-38. Retrieved from <http://www.sciencedirect.com/science/article/pii/S1051137713000557>
- 8 Bolotnyy, V. (2014), The Government-Sponsored Enterprises and the Mortgage Crisis: The Role of the Affordable Housing Goals. Real Estate Economics, 42: 724-755. Retrieved from <http://onlinelibrary.wiley.com/doi/10.1111/1540-6229.12031/abstract>
- 9 Min, D. (2011). *Faulty Conclusions Based on Shoddy Foundations: FCIC Commissioner Peter Wallison and Other Commentators Rely on Flawed Data from Edward Pinto to Misplace the Causes of the 2008 Financial Crisis* (Rep.). Retrieved from <https://www.americanprogress.org/wp-content/uploads/issues/2011/02/pdf/pinto.pdf>
- 10 Weicher, J. C. (2010). The Affordable Housing Goals, Homeownership and Risk: Some Lessons from Past Efforts to Regulate the GSEs. Retrieved from: <https://files.stlouisfed.org/files/htdocs/conferences/gse/Weicher.pdf>
- 11 Edelman, C. M. (2017). The 2008 Housing Crisis. Retrieved from <https://www.americanprogress.org/issues/economy/reports/2017/04/13/430424/2008-housing-crisis/>

- 12 Weicher, J. C. (2010). At the HUD of the Fall. Retrieved from <http://www.nationalreview.com/article/226163/hud-fall-john-c-weicher>
- 13 Sanchez, D. (2016). No, Lending To Poor People Did Not Cause The Financial Crisis. Retrieved from <https://thinkprogress.org/no-lending-to-poor-people-did-not-cause-the-financial-crisis-8ba95ce23015/- .y9zv46oot>
- 14 Johnson, L. (2013,). Elizabeth Warren Destroys Financial Crisis Myth. Retrieved from [http://www.huffingtonpost.com/2013/10/29/elizabeth-warren-financial-crisis\\_n\\_4174123.html](http://www.huffingtonpost.com/2013/10/29/elizabeth-warren-financial-crisis_n_4174123.html)