BY BILL BERLINER

Final Thoughts

This will be my last column for *Asset Securitization Report*. I'd like to leave readers with some parting thoughts on the current regulatory and policy environment and its impact on consumer mortgage rates.

I read with interest the article in the Christmas Eve edition of the *Wall Street Journal* entitled "Push for Cheaper Credit Hits Wall," which indicated that the **Federal Reserve**'s desire to push primary mortgage rates lower has been derailed because "... a shift in the lending landscape has made some banks unable, or unwilling, to pass along cheaper credit." The article cites a variety of factors, including a shift in lenders' cost structure and their hesitance to add processing capacity.

In my mind, the unwillingness of lenders to add capacity and offer aggressive pricing is a totally rational response to a regime in which prices for a variety of inputs have been massively skewed by government actions. The most obvious factor distorting the market is the Fed's latest round of quantitative easing, the indefinite purchase of $40 billion in mortgage-backed securities (MBS) a month, which represents between one-third and one-half of the industry's gross production.

As a result, the spread between the MBS current coupon rate and the 10-year Treasury is half of where it was last summer, before the Fed's intentions to manipulate MBS prices became clear.

Few lenders will want to hire additional personnel and increase processing capacity when the prices at which they can sell their production are subject to the whims of Fed Chairman **Ben Bernanke** and a handful of Open Market Committee members.

An even more egregious distortion is the pricing of guarantee fees by the Government Sponsored Enterprises (GSEs). As prompted by the **Federal Housing Finance Agency**, g-fees have increased by 20 basis points since the end of 2011, and are expected to continue to rise next year. Rising g-fees have been a major factor in keeping primary rates at artificially high levels. Combined with the GSEs' continued overpricing of g-fee buydowns (as discussed in my October column), each 10 basis point increase in g-fee fees translates into a 30-35 basis point increase in primary mortgage rates. This has offset much of the benefit of the Fed's MBS purchases and is a primary culprit in the failure of primary rates to decline.

Moreover, the increase in g-fees represents a pointless distortion of market pricing. G-fees no longer reflect the riskiness of the loans being insured. Rather, their pricing represents the highly questionable notion that if they are increased enough, a "level playing field" will cause a flood of private capital to flow into the MBS markets, resulting in a resurgence of private-label issuance.

The notion that higher g-fees will on their own lead to a revival of the private-label MBS market is a fantasy. There are numerous factors impeding the lack of a recovery in non-agency issuance, including implementation of several Dodd-Frank Act provisions, the impact of Basel III rules, and the lack of a credible rating system. As a result, the GSEs are not going anywhere in the near future, as there is simply nothing on the horizon that can replace their role. It is ironic that, five years after entering conservatorship and costing U.S. taxpayers more than $150 billion, **Fannie Mae** and **Freddie Mac** are more entrenched than ever.

On a parting note, regulators and policy makers would do well to heed the words of Albert Einstein, who said that "any intelligent fool can make things bigger and more complex. It takes a touch of genius and a lot of courage to move in the opposite direction." Thanks to SourceMedia for providing me with this platform for the last four years, and to Karen Sibayan for her work as my editor.

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