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Before the U.S. Senate

Committee on Banking, Housing, and Urban Affairs

Hearing on March 27, 2019

Chairman Crapo, Ranking Member Brown, members of this committee, my name is Michael Bright and I represent the Structured Finance Industry Group, or "SFIG." On behalf of SFIG and its thousands of members in the securitization industry, I very much appreciate the opportunity to speak to you today.

SFIG was formed in 2013 with the goal of convening the many diverse institutions involved in securitization – including consumer and commercial lenders, data providers, auto and equipment finance companies, rating agencies, law firms, trustees, banks, and – very importantly – end investors[1]. This structure forces SFIG to convene all parties - both those involved with the creation of a fixed-income security and those who invest in them. When SFIG takes a position, we have a broad range of perspectives incorporated into our view. Since SFIG represents all participants in a transaction, long-term financial stability – in the mortgage market as well as other markets - is a core principle of ours[2].

The purpose of today's hearing is to discuss reform of our nation's secondary mortgage market. I thank Chairman Crapo and many other members of this committee for their continued work on this issue. The latest outline touches upon many of the principles that are important to SFIG, including: creating a clear role for private capital, establishing a clear and explicitly defined role for the government, the preservation of a liquid TBA market, the preservation of a 30-year fixed rate mortgage, and making use of already-existing securitization infrastructure[3].

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[1] "End investors" includes firms such as: asset managers, life insurance companies, and pension funds.
[2] SFIG's governing bylaws go to great lengths to differentiate its operating rules from those of other trade associations. A policy position is only advocated by SFIG if consensus is achieved by all relevant members of a committee, and each committee has representation across all relevant aspects of such market. This natural tension is an important governor on SFIG's policy positions and supports longer-term, market-wide solutions.
[3] The agency and government mortgage markets both rely on securitization, as the basic function of the GSEs and Ginnie issuers are to finance operations through the transformation - or securitization - of mortgage loans into

There is a substantial ongoing role for Congress to help finish the job of housing reform for many reasons. First, as the former head of Ginnie Mae, I can attest that global investors will allocate much more capital and at a much lower cost to the US mortgage market if Congress puts a seal of approval on a new end state. One major lesson I learned at Ginnie is that, when speaking to a non-US investor, the first thing they will ask is, "Is the law clear?" Any lack of clarity on the government's role versus private capital's role adds ambiguity, and ambiguity adds to costs[4]. These costs are ultimately borne by the homeowner. There are many additional considerations relating to the use of Ginnie Mae, and I am happy to discuss those with you in more detail.

Additionally, as I said to this committee when I appeared before it in 2018, we have a housing affordability crisis in our country, both in rental and homeownership. Over the past decade asset prices have increased substantially faster than wages. This creates an imbalance in our economy that is felt particularly strongly in the housing sector. SFIG membership supports, and wants to help provide, broader accessibility to mortgage credit throughout the country. Ultimately, a role for Congress here is critical.

Going forward, SFIG believes that private capital can, and should be, productively channeled to further sound public policy objectives. Private capital is today very much available to support America's housing market and to augment the role of the GSEs and the FHA.

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mortgage-backed securities. Building off what already exists the way the Chairman's outline suggests is a sensible approach.

[4] Global investors account for a larger and larger share of U.S. MBS purchases, especially as the Fed winds down its balance sheet.

Today private investor appetite for mortgage credit risk is counted in the tens of billions of dollars per month. Insurance companies, for example, had roughly $500 billion of residential whole loans on their balance sheet at year-end 2017, and this number has been growing. $50 billion of non-agency PLS[5] was issued in 2018, and this number continues to grow as well. Non-agency whole loan sales have been comparable in size. CRT[6] transactions have also provided roughly $70 billion of <u>first loss</u> private capital to the market to-date[7]. The pool of additional private capital is today quite deep.[8] Reform should build upon this dynamic so that private capital can help enhance safe and responsible access to mortgage credit within the guardrails established by law and the CFPB.

As we seek to enhance the role of private capital, I would like to cite three issues that we suggest Congress address.

Number one, an event that looms on the horizon is the end of the so-called "QM patch" in 2021. Private capital can absolutely help to fill in once this transpires, but some policy changes would be very helpful to ensure the continued availability of mortgage credit. <u>Most importantly, there needs to be a process of determining what qualifies for QM that is independent of whether</u>

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[5] "PLS" is short for "private label securitization", or a security that is issued by a company other than a GSE and does not have FHA insurance.
[6] This includes all credit risk transfer ("CRT") transactions done to-date by the enterprises.
[7] This $70 billion in first loss capital stands in front of nearly $2 trillion in total mortgage unpaid principal balance (UPB).
[8] For example, see: https://www.wsj.com/articles/private-investors-encroach-on-fannie-and-freddies-domain-11552132801?shareToken=st1e2068f01cbd4b87a1595cef380c53ed&reflink=article_email_share

or not the GSEs' underwriting systems accept the loan. There are numerous ways this could be done, and I would be happy to discuss some of those ideas in further detail if you would like[9].

Number two, policy makers should strive for better alignment of regulatory capital requirements between the GSEs and banks. For example, the GSEs get substantial capital relief - and rightly so – for the credit risk transfer transactions they issue. Banks, however, do not. By allowing banks to make a loan, hold it on balance sheet, and – if they choose – hedge some of the credit risk in return for appropriate capital relief – bank lending can play a more prominent role in our mortgage market and help fill in where sometimes the GSEs cannot.[10]

Finally, as policy-makers look to reduce total reliance on Fannie, Freddie and FHA while ensuring access to homeownership, a proper mechanism for allowing REITs to access the Home Loan Bank system makes sense.[11]

There are, of course, many more challenges to discuss. In the meantime, Mr. Chairman, I want to thank you again for continuing to work on this important issue. We look forward to working with you and with everyone on this committee to ensure that our country's secondary mortgage market can better serve all Americans.

Thank you.

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[9] See, for example: https://www.urban.org/research/publication/what-if-anything-should-replace-qm-gse-patch.

[10] The ECB has recently made substantial strides on this for European banks, and SFIG believes that US regulators should follow suit. See: https://eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/draft-guidelines-on-significant-risk-transfer-srt-for-securitisation-transactions/-/regulatory-activity/press-release

[11] If properly capitalized, REIT borrowing from the Home Loan Banks via collateralized loans represents materially less risk to the taxpayer than selling to FHA, Fannie, or Freddie, and the existing rules that effectively bar REITs should be re-examined.