EXTENSIONS OF REMARKS

CAPITAL MARKETS

HON. MAX SANDLIN

OF TEXAS

IN THE HOUSE OF REPRESENTATIVES

Thursday, May 18, 2000

Mr. SANDLIN. Mr. Speaker, Frank Raines, Chairman and CEO of Fannie Mae, testified this week before the House Banking and Financial Services Subcommittee on Capital Markets. His testimony was interesting and informative, and I appreciated hearing from him. So that those who will not receive a copy of his testimony may understand more about what Fannie Mae does, and what Mr. Raines' views are, I include for the CONGRESSIONAL RECORD a copy of his speech before The National Press Club on May 12.

REMARKS PREPARED FOR DELIVERY BY FRANKLIN D. RAINES, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, FANNIE MAE

Thank you for joining us today.

These are ''interesting'' times for the housing industry, and we wanted to bring you up to date since Jim Johnson gave his farewell address as Chairman of Fannie Mae from this podium in November of 1998. A year and a half may not seem like a long time, but it has been an unusually turbulent period, and much is at stake.

As some of you may recall, Jim titled his speech, ''Why Homeownership Matters—Lessons Learned from a Decade in Housing Finance.'' He painted a very positive picture. He said the American Dream of homeownership was more alive, achievable and inclusive than ever. He said the growth in homeownership is making everything better, from the wealth of average families, to the health of older communities, to the strength of the nation's economy. The housing finance system, he declared, was the most efficient and effective ever devised.

Jim was absolutely right. And things have gotten even better. The national homeownership rate has just topped 67 percent, a new record. Even though mortgage rates have gone up, the housing market remains robust. Housing starts are strong. Home sales are vigorous. Home values are appreciating. Households are growing. Homes are getting larger. Home equity is rising. Default and foreclosure rates are at historic lows.

And the process of buying a home has never been better. Automated underwriting and other advances have made it faster, easier, less frustrating and less costly to finance a home, and reduced the bias in lending decisions. E-commerce and financial deregulation are giving consumers more power and more choices at lower costs. The mortgage industry has been breaking through the old red lines and bringing affordable housing finance to families that used to be overlooked, neglected or rejected.

Behind all of this, the secondary mortgage market—including Fannie Mae—is attracting billions of dollars of private capital from all over the world, providing lenders with a steady flow of funds in all communities at the lowest rates in the market and with zero risk to the government.

With the system we have today, and with the economic winds at our backs, the national homeownership rate could rise as high as 70 percent in this decade, with ten million new homeowners and growth especially among minorities, new Americans and other historically underrepresented consumers.

Yogi Berra warned that, ''A guy ought to be very careful in making predictions, especially about the future.'' But I think we're on pretty solid

But I stand before you at a moment when questions have been raised about the utility of the U.S. secondary mortgage market that is so integral to the system's functioning as a whole. Some of these inquiries are well meaning. But it is no secret that some of the questions are generated by financial competitors that would earn more if Fannie Mae and Freddie Mac were not lowering costs for consumers.

The U.S. housing finance system is strong, but it is not indestructible. Changing it significantly could have real consequences for real families. The burden of proof for anyone that wants to change the system is a simple but stringent test—does it help or hurt home buyers?

Today, let me reinforce why our system works so well and what we are up against.

To illustrate what is so good about our system, let's compare it to the other major industrialized countries. Most of the G–7 countries have a well-developed mortgage system organized around depository institutions. But the mortgages they offer are less consumer-friendly. In America we take the 30-year, fixed-rate mortgage for granted. Last year, 66 percent of the mortgages issued in the U.S. were 30-year, fixed-rate conventional mortgages.

Outside the U.S., the long-term fixed-rate mortgage is a rarity. In Canada, they have rollover mortgages, where the rate is fixed during the first one to five years, with a prepayment penalty equal to three months of interest. The fixed-rate term in Spain is usually one year. In France, 80 percent of all mortgages have variable rates. In Germany, you can get a fixed-rate for five to fifteen years, but you can't refinance during this period without paying a huge penalty.

The low down payment features of U.S. conventional mortgages are also unique. We now take for granted down payments as low as 5 and 3 percent. That's not the case in, say, Germany, France, the United Kingdom or Japan. In Germany, the down payment is typically 30 to 40 percent, and in Japan, you've had to put down effectively 50 to 60 percent.

Why are American conventional mortgages more consumer-friendly? Mainly because we have a secondary mortgage market. In other countries, the banks largely make the loans from their deposits and hold the mortgages as an investment. Our system primarily worked that way until the 1970s and 1980s. Today in America, banks, thrifts, mortgage bankers and credit unions make the loans, but they can depend on the secondary market to supply the long-term funding.

What Congress did in establishing a secondary market in the thirties and privatizing this market in the sixties made this change possible, and it has turned out to be absolutely brilliant. When it chartered Fannie Mae and then Freddie Mac as private companies, it created a system that harnesses private enterprise and private capital to deliver the public benefit of homeownership. And it maximizes this public benefit while minimizing the public risk, without a nickel of public funds.

Let's do a quick risk-benefit analysis, starting with the risk side of the equation.

There is a simple reason fixed-rate mortgages with low down payments are rare outside the U.S. Since they don't have a secondary market to buy the mortgage, the lender has to hold the loan and take on all the risk. That is, the lender has to assume the credit risk—the risk that the borrower could default—and the interest-rate risk—the risk that interest rates will change and cause the lender to pay out more to depositors than he is receiving on loans. So the lender protects himself by requiring the consumer to pay more up front and more each month if interest rates rise.

In America, the secondary market purchases the mortgage, taking most of

This process is called ''risk transformation.'' Here's how it works. Fannie Mae and our lender partners create mortgages that consumers want, like our 3 percent down Fannie 97. And we finance them with capital we raise by creating debt instruments that investors want, like our Benchmark securities. We share the credit risk on the Fannie 97 with mortgage insurance companies, and we hedge the interest rate risk by selling callable debt securities to Wall Street. We also work with Wall Street to develop even more refined strategies for hedging our interest-rate risk and credit risk. Last year, we spent about half of our gross revenues paying others to assume risk we didn't want.

Managing risk, in fact, is all we do. We manage risk on one asset—U.S. home mortgages—perhaps the safest asset in the world. All told, 96 percent of all mortgages in America are paid in a timely fashion, which goes to show just how much Americans cherish homeownership. And to help us analyze our risk precisely, we have amassed performance data on 29 million loans dating back over 20 years.

All of this helps to explain why our credit loss rate during the nineties averaged only 5 basis points—five cents on every hundred dollars—even during the recessions in California and New England. Just to compare, the bank credit loss rate on their more diverse set of assets was an average of 86 basis points, or 86 cents on every hundred dollars. Today, our loss rate is lower than ever, at just 1 basis point last year.

A strong secondary market makes the entire financial system safer and more stable. The government holds Fannie Mae and Freddie Mac to the highest financial safety and soundness standards in the financial services industry. We have to hold enough capital to survive a stress test—essentially, ten years of devastating mortgage defaults and extreme interest rate movements. Other financial institutions would not last long under the scenario spelled out in our capital requirements. Thrifts, for example, would become insolvent after five to seven years. At the end of the ten years, Fannie Mae and Freddie Mac would be the only major holder of mortgage assets still standing. A strong secondary market puts mortgages in the safest hands.

Now let's look at the public benefit.

First, the secondary market means consumers never have to hear their lender say, ''sorry—we're out of money to lend.'' People think this can't happen, that it's something out of the Depression era. But without Fannie Mae and Freddie Mac, this could have happened at least twice in the last 20 years. When the S&L system crashed during the eighties, the thrifts in California and Texas would have had no money to lend if we had not stepped in to back their loans. Then, in 1998 when a credit crisis shook the capital markets, conventional mortgage rates would have jumped as jumbo rates did if Fannie Mae and Freddie Mac hadn't been able to raise billions of dollars in capital, and keep it flowing to lenders. Home buyers never felt the credit crunch. In both cases, hundreds of thousands of families would have been denied a mortgage.

The secondary market also drives down mortgage costs. Last week, a mortgage backed by Fannie Mae would be $19,000 cheaper, over the term, than a jumbo mortgage that's just a dollar beyond our loan limit. Our savings over the jumbo market jumped beyond $26,000 during the credit crisis of 1998. Today, a Fannie Mae loan is about $200,000 cheaper than a subprime mortgage, and even about $18,000 cheaper than an equivalent FHA or VA loan backed by the government. During the nineties, Fannie Mae alone saved consumers at least $20 billion through lower mortgage rates.

The secondary market also expands homeownership. Under the 1992 revisions to our charter, Congress requires Fannie Mae and Freddie Mac to meet affordable housing goals, to devote a set percentage of our business to underserved families and communities. As many of you know, Fannie Mae

Since 1993, these initiatives have boosted our lending to African Americans by 31 percent, and to all minorities by 16 percent. Last year, Fannie Mae alone provided nearly $46 billion in housing finance for over 400,000 minority families. That's what having a strong secondary market can do.

The success of our housing finance system is not lost on the other major industrialized countries. I just returned on Tuesday from meetings in London and Frankfurt with our debt investors—the people who buy our Benchmark securities that allow us to finance mortgages here. One of the many ironies of being Chairman of Fannie Mae is that there are countries in which investors will help finance American homeownership while their own homeownership rate is lower.

Naturally, many countries are curious about our system. Fannie Mae has responded to many requests to serve as advisors overseas, not because we will ever buy loans abroad, but because of our expertise in the unique U.S. secondary market, a market that is viewed in other countries as some kind of miracle.

So over the past few years, a team from Fannie Mae has been invited to 29 different countries from Europe, to Africa, to Latin America, to Asia to help them figure out how to build a better system like ours. These countries have asked us how to deepen their capital markets, manage risk better and expand affordable lending and fair lending. We just had a team in South Africa to help a start-up secondary market conduit develop mortgage risk modeling, which they want to use to fight redlining.

What you see in America is a dynamic web of entities—both public and private sector—delivering homeownership to citizens of all backgrounds, incomes and circumstances. We have small, medium and large mortgage originators and lenders, serving consumers from store fronts to web sites. We have home builders, Realtors, mortgage brokers, mortgage insurers and appraisers and mortgage.coms. We have consumer advocates, citizen activists and nonprofit housing organizations. The system receives wide support from local, county, state and federal agencies and elected leaders, public policies and public benefits. And behind all of it, we have a vibrant secondary market drawing capital from all over the world to finance this homebuilding, lending and purchasing.

The interaction of these entities is constantly driving the housing system to improve itself, to reward low cost and high quality, to police the bad actors and chuck out the bad apples, to search for new markets and untapped home buyers, and break down the barriers. Looking back over my years in the industry gives me confidence that the U.S. housing system, with a little nudging here and there, will continue to do the right thing for consumers. Good money will drive out the bad. A better mousetrap is always in development. Underserved families will be served. Our system is constantly evolving and innovating to make owning a home more possible for more people.

Given how great our system is, it makes you wonder: Why are some voices suggesting there is something wrong with our housing finance system, something fundamental that needs to be fixed?

Certainly, the system benefits from constructive scrutiny. It is entirely appropriate for the Congress to hold oversight hearings on the safety and soundness of the secondary mortgage market. I look forward to testifying before Mr. Baker's subcommittee next week. It is also appropriate for our regulators—HUD and OFHEO—to monitor us closely. And it is appropriate for other agencies to ask questions within their purview as well. We welcome official scrutiny.

But something less constructive is also going on here in Washington. Recently, a senior Senator asked me why Fannie Mae was suddenly in the news so much. I explained to him that some very large financial institutions have decided they are not content with the way the system works for them. They see how Fannie Mae and Freddie Mac drive down mortgage costs for consumers and serve all mortgage lenders. They see how we give small- and medium-sized mortgage lenders a chance to compete with the large institutions. So this small group of large institutions would like to eliminate the benefits that Fannie Mae and Freddie Mac provide, from low-cost financing to automated underwriting systems.

They have brought the fight to Washington under the name FM Watch. They began by defining themselves as a watchdog group, and their rhetoric was mild. But over the course of the past year, they have been unable to gain any traction. They have been unable to answer the question of how the consumer would benefit from any of their proposals regarding Fannie Mae and Freddie Mac. And our nickname for this group, the ''Coalition for Higher Mortgage Costs,'' has stuck like a tattoo.

So this group has switched from watchdog to attack dog. Its strategy is now to create an instant crisis, to convince policymakers that Fannie Mae and Freddie Mac are a financial risk to the taxpayer, an S&L crisis waiting to happen. This is the equivalent of the owner of one movie theater going to a rival theater and shouting ''fire!'' A mortgage insurance industry that nearly collapsed in the 1980s and a banking industry that collapsed in the early 1990s now seek to tag the secondary mortgage industry with the word ''risky.''

By trying to create a crisis, FM Watch has gone beyond a watchdog role into an approach which, carried to its logical conclusion, would actually harm the housing finance system, all in an effort to create short-term advantages for its members.

Never mind that its claims collapse under scrutiny. Fannie Mae and Freddie Mac are far from the S&L problems and banking problems that bankrupted their deposit insurance funds and required federal direct and indirect bailouts. To the contrary, if the failed S&Ls and banks had stuck to safe mortgage investments like we do instead of all their speculative non-mortgage investments, they might not have failed.

Our safety and soundness allowed us to be the ''white hats'' in the S&L and banking crises as we rode in with additional capital to keep the housing system going. The risk-based capital standard that Congress gave us since the S&L and banking crises has made us even more safe and sound. What FM Watch does not mention is that if the economic stress test in our capital standard ever came to pass, the government would have to bail out their members long before Fannie Mae was in any danger.

But you can learn a lot from debating with an entity like FM Watch. They use so many facts that you just can't find anywhere else. It reminds me of a story Adlai Stevenson once told. He reminded his audience of the old lawyer addressing the jury, who closed his summation by saying: ''And these, ladies and gentlemen, are the conclusions on which I base my facts.'' FM Watch is looking for any conclusion that will help to damage Fannie Mae and Freddie Mac. The facts will be altered to fit.

If this Coalition for Higher Mortgage Costs were successful, it would destabilize the secondary mortgage market and the related capital markets. This destabilization would undermine the entire housing industry and its progress, raise costs for consumers and stifle the advance of homeownership—harming underserved families first. Because such an outcome is unacceptable, I don't think this will happen. The American people and their elected representatives are smart. They will soon recognize another lobbyist-driven Potemkin-crisis public relations campaign for what it is. Then they and the capital markets will stop listening.

Certainly our housing system is not perfect. Minority homeownership rates are too low. There is still inequality in affordable mortgage credit. Too many families that can afford the least are being charged the most for mortgage

One issue deserving of further study is the question of why disparities in loan approvals between white and minority borrowers continue to persist. Many have suspected overt racial discrimination. But those disparities can be found even in automated underwriting systems using racially neutral underwriting criteria.

We take this issue very seriously because in our experience, automated underwriting has in fact expanded lending to minority families. To try to understand the problem better, we have studied results from our system, Desktop Underwriter. We found that differences in credit histories account for about 50 percent of the difference in loan approvals. And when you also factor in the applicant's loan-to-value ratio and reserves, these three factors together account for over 90 percent of the difference in the approval ratings. The results of this study point to the need for public policies addressing consumer credit education and minority savings and wealth development.

The housing finance system needs more answers to questions such as this. To further explore these issues, next month Fannie Mae is hosting a conference titled ''The Role of Automated Underwriting in Expanding Minority Homeownership.'' We're bringing together a range of advocates, academics, regulators and lenders to engage in a meaningful dialogue concerning automated underwriting systems and their role in expanding homeownership and promoting fair lending. I am personally committed to working every day to make sure that these systems are the best they can possibly be.

All in all, the housing finance system—through inspiration, perspiration and a little luck—has grown into the most successful system in the world. It is worth protecting and defending. We must never allow the system to be damaged by those who would place their narrow financial interests ahead of those of the industry as a whole and—most importantly—ahead of the consumers we serve.

This being a national election year, it is a good time to discuss and debate our national priorities, and certainly homeownership is high among them. Few ideals unite us more than owning a home to raise your family, invest your income, become part of a community and have something to show for it. There are many ways to go about improving the housing finance system to make it better, more affordable and more inclusive. As we pursue these efforts, we need to keep our eyes on the prize and ask the most important question, ''does this proposal help or hurt home buyers?''

Thank you.

HONORING AMBASSADOR STEPHEN CHEN

HON. SOLOMON P. ORTIZ

OF TEXAS

IN THE HOUSE OF REPRESENTATIVES

Thursday, May 18, 2000

Mr. ORTIZ. Mr. Speaker, today I pay homage to an outstanding diplomat who is leaving Washington with two years of distinguished service in the United States Diplomatic Corps, Ambassador Stephen Chen.

Ambassador Chen has been a wealth of information for me and my staff about the intriguing diplomacy of the Pacific Rim. He leaves Washington with the satisfaction of having represented the interests of his country well while in the United States, and he strengthened the all-important relationship between the United States and Taiwan.

Ambassador Chen is a career officer, serving Taiwan's foreign ministry for nearly 50 years now. He is the consummate diplomat, with a rare gift of persuasion without the appearance of appearing to be inflexible. He has charmed many Washington officials, guests and other diplomats during his time here with insightful knowledge about trade, international relations, and a variety of other topics.

At Twin Oaks, a historic landmark in central Washington, Ambassador Stephen Chen and his lovely wife Rosa have hosted many gatherings. Ambassador Chen is always generous in regaling his guests with self-deprecating jokes, as well as stories about Taiwan and her people. He brought all of us closer to Taiwan and to his native culture.

I ask my colleagues to join me in wishing Stephen and Rosa Chen well as they retire from the foreign service and return to their beloved Taiwan.

HONORING THE LATE EVANGELINE C. MILLS

HON. SAM FARR

OF CALIFORNIA

IN THE HOUSE OF REPRESENTATIVES

Thursday, May 18, 2000

Mr. FARR of California. Mr. Speaker, today I honor a woman who supported countless local charities in the community. Mrs. Evangeline C. Mills passed away at the age of 69.

Born in Holtville on November 22, 1930, Eve lived in Salinas for 46 years. She played a very active role in the community including her membership on the advisory board of the Foundation for Monterey County Free Libraries, on the board of the Western Stage and also as past president of PEO, a women's philanthropic organization. In 1996 Eve and her husband were named Volunteers of the Year by the United Way of Salinas Valley where they served as co-chairs of the Alexis de Tocqueville Society. In the same year, the Development Executives Network and the National Society of Fund-rasing Executives, Monterey Bay chapter, honored the couple as Philanthropists of the Year. Eve was also a volunteer driver for Meals on Wheels of the Salinas Valley for over 20 years.

Eve will be forever remembered by dear family and friends. She will be sorely missed by the many people who were privileged to know her. Eve is survived by her husband; two sons, David and Jim Mills, both of Salinas; two daughters, Susan Mills of Salinas and Kathy Mills of Pacific Grove; her parents, Ted and Loreen Todd of San Jose; and eight grandchildren.

HONORING GEORGIA GULF CHEMICALS & VINYLS, L.L.C.

HON. KEN BENTSEN

OF TEXAS

IN THE HOUSE OF REPRESENTATIVES

Thursday, May 18, 2000

Mr. BENTSEN. Mr. Speaker, I rise to congratulate Georgia Gulf Chemicals & Vinyls, L.L.C. and its employees for selection by the Pasadena Chamber of Commerce as the Industry of the Year.

Georgia Gulf and its employees have been responsible members of the Pasadena community, and have had a significant impact on the local business community. In addition to making sizable expenditures on supplies and raw materials in the Pasadena area, Georgia Gulf has shown a commitment to reducing the amount and/or toxicity of hazardous and non-hazardous wastes generated. Though not required by any state or federal regulations, Georgia gulf operates a vapor recovery system for acetone loading, resulting in reducing emissions to the atmosphere.

Georgia Gulf received recognition from Pasadena's Local Emergency Planning Committee for their support and involvement with the Household Hazardous Material Collection Day. Georgia Gulf employees also volunteer with the Bay Day Celebration to provide information to the public on pollution prevention, water quality, and the Galveston Bay ecosystem.

In addition to environmental efforts, Georgia Gulf has shown a commitment to safety. The company received the Texas Chemical Council's ''Caring for Texas'' Award for outstanding performance in pollution prevention, community awareness, and safety awareness. The Council also recognized Georgia Gulf for going a year without a recordable accident in 1999.

A true connection exists between Georgia Gulf and the Pasadena community. Most of the 80 employees make their homes in Pasadena area neighborhoods. Demonstrating their generosity and connection to community, the company's employees have logged thousands of volunteer hours on local projects.

Georgia Gulf's active involvement in the Pasadena community can be traced through its participation in a wide variety of civic organizations, including the Pasadena Chamber of Commerce, the Pasadena Citizens Advisory Panel, the Clean Channel Association and several community-based nonprofit organizations. The Pasadena Livestock Show and Rodeo and area Little Leagues also benefit from the active support of Georgia Gulf. The employees' participation in the American Heart Association's Heartwalk, United Way fund-raising, and the Bridge to help battered women, add to the list of reasons why Georgia Gulf has earned this year's Industry of the Year Award.

Georgia Gulf has contributed to efforts to provide a first-rate education for the young people of Pasadena. Georgia Gulf and its employees: serve on the East Harris County Manufacturers Association Schools Outreach Subcommittee to provide Pasadena schools with supplies, mentoring, and monetary donations; host industry tours for ninth graders from area high schools; participate in a mentoring program with fifth graders called the Pen Pal program; and donate computer equipment to the Pasadena school district.

Mr. Speaker, I congratulate the employees of Georgia Gulf on being named the Pasadena Chamber of Commerce Industry of the Year. This honor is well-deserved for their work in expanding business and job opportunities, establishing safer conditions for workers, and instituting initiatives to protect the environment. This award indicates that Georgia Gulf has demonstrated a commitment to strengthening community relations by supporting employees volunteer activities and making contributions to deserving sectors of the community.