

**Chicago**  
**Federal Home Loan Bank**



**Thoughts on Comparative  
Housing Finance Systems**

**Alex J. Pollock**  
**March 23, 2004**

# U.S. Homeownership Rates

<b>1900</b>	<b>47%</b>
<b>1940</b>	<b>43%</b>
<b>1980</b>	<b>65%</b>
<b>1995</b>	<b>65%</b>
<b>2000</b>	<b>67.7%</b>
<b>2003</b>	<b>68.6%</b>

# Top Ten Countries: Homeownership Rates



<b>1. Spain</b>	<b>81%</b>
<b>2. Ireland</b>	<b>80%</b>
<b>3. Greece</b>	<b>78%</b>
<b>4. Norway</b>	<b>76%</b>
<b>5. Portugal</b>	<b>76%</b>
<b>6. Belgium</b>	<b>74%</b>
<b>7. New Zealand</b>	<b>71%</b>
<b>8. Australia</b>	<b>70%</b>
<b>9. United Kingdom</b>	<b>69%</b>
<b>10. United States</b>	<b>69%</b>

Sources: International Union for Housing Finance, 2001;  
European Mortgage Federation, 2002

# Comparative Mortgage Finance: Distribution of Risks Perspective

## I. The Risks Exist

## II. The Questions:

-- Who bears them now?

-- Who should bear them?

-- Who is best equipped to bear them?

## III. Mortgage Finance Systems = Different patterns of risk distribution

# Who Has the Interest Rate/Prepayment Risk?

- ◆ Variable Rate Mortgages
  - ◆ Mark-to-Market Prepayment Fees
- } Borrower
- ◆ Bond-Based Systems
  - ◆ Pass-Through MBS
- } Capital Market Participants
- Also:
- ◆ Deposit Insurance
  - ◆ GSE Balance Sheets
- } Government Support\*

**\*Fundamental risk: Money printing behavior of the government's central bank – poetic justice?**

# Historical Example

## Real Estate Lending Limits for U.S. National Banks Under the McFadden Act (1927)

**Advance &  
Maturity Limits:**                      **50% LTV Max. &  
5 yrs. on improved real estate**

**Lending Limit:**                      **Greater of:  
25% of capital  
or  
50% of savings deposits**

# A Long-Term Financial Regime Shift

## Post–War Structure

- ◆ Deposits/Savings & Loans
- ◆ Interest Rate Ceilings
- ◆ Bretton Woods/Fixed Exchange Rates
- ◆ International Trade
- ◆ Housing Finance Credit Crunches

## Current Structure

- ◆ Capital Markets/GSEs
- ◆ No Interest Rate Ceilings
- ◆ Floating Exchange Rates/Fiat Currencies
- ◆ Advanced Globalization
- ◆ Housing Finance Robust

# Mortgage Funding Structures

## Deposit Financed

- ◆ Banking model
- ◆ Contract savings model

## Bond Market Financed

- ◆ Mortgage bond model
- ◆ MBS model

# Bond-Based Models

**American GSEs efficiently link  
long-term residential mortgages  
with the bond markets.**

**So do other models.**

# Strengths of Bond-Based Systems

(e.g., European Mortgage Banks and American GSEs)

- ◆ **Specialized institutions viewed as lower risk**
  - More transparent
  - Separate and specialized regulatory focus
- ◆ **Focus on pure mortgage finance**
- ◆ **Ability to tap capital market funding**
  - Source for longer term fixed-rate funds
- ◆ **Tested Model**
  - 200 years in Denmark, 100 years in Germany, 70 years in the U.S.

# Mortgage Bond Issuers

- ◆ **More than 70 mortgage bond issuers in the European Union**
- ◆ **In most members states, mortgage bond issuers are credit institutions**
- ◆ **The right to issue is confined to specialized credit institutions in most countries**

**Source: European Mortgage Federation**

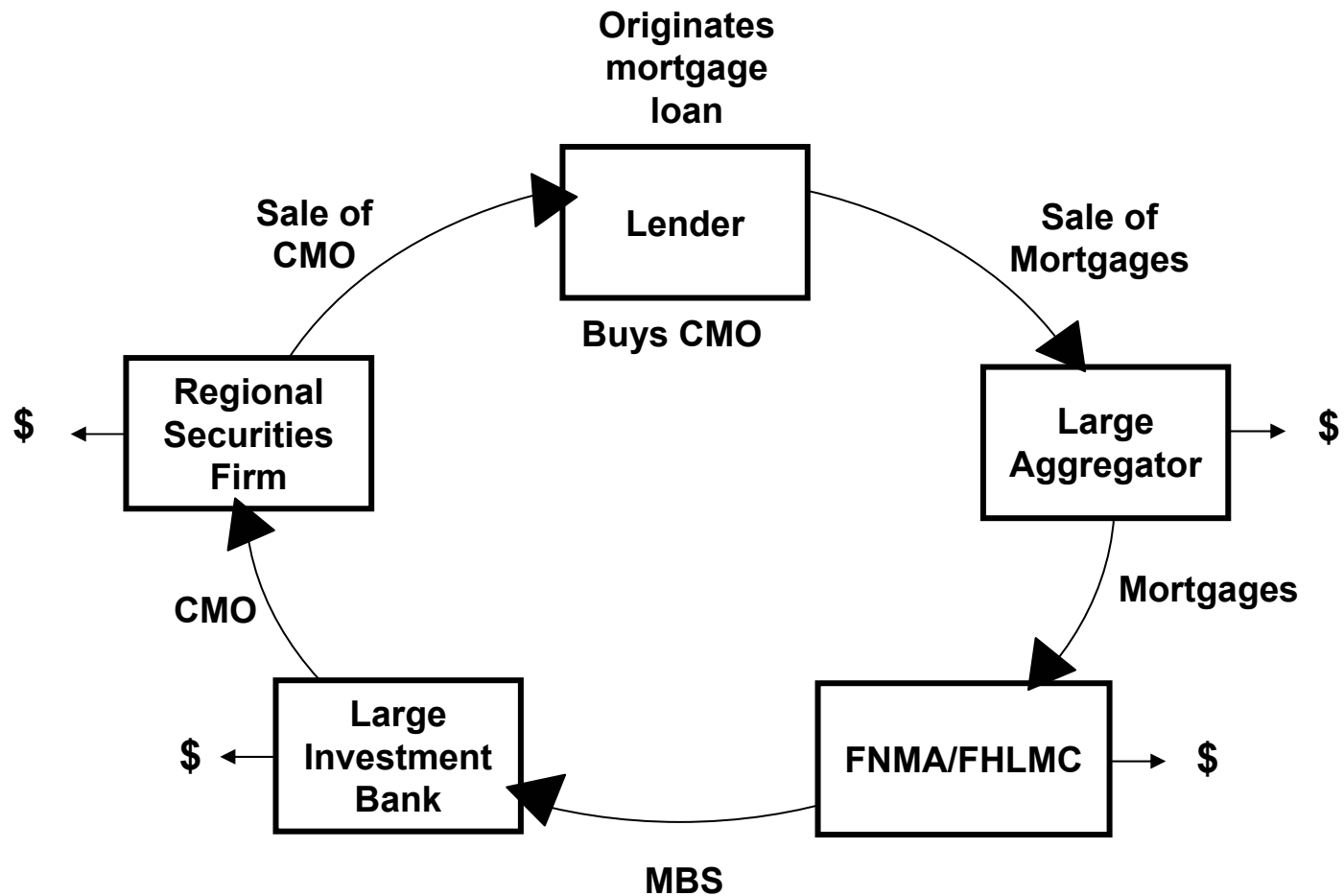
# U.S. System: More Competition Is Needed

## 2002 Return on Common Equity

<b>Freddie Mac</b>	<b>28.3%</b>
<b>Fannie Mae</b>	<b>25.8%</b>
<b>Commercial Banks</b>	<b>14.9%</b>
<b>Thrifts</b>	<b>13.7%</b>
<b>Chicago FHLB</b>	<b>9.7%</b>
<b>FHLB Average</b>	<b>5.0%</b>

Sources: Fannie Mae & Freddie Mac Investor/Analyst Reports; FDIC Quarterly Banking Profile, Savings Institutions & Commercial Banks, <http://www2.fdic.gov>; Federal Housing Finance Board

# U.S. System A "Circle of Value"





# **The International Dialogue: All Systems Can Be Improved**