

Banking by David Goldman

Mortgage boom collapses, as planned

Restrictions on government-financed mortgages will drastically reduce the issue volume.

The American debt expansion during 1985-86 was supported by two less-than-invisible hands.

The first was the growth of off-balance-sheet liabilities; the second was "off-budget borrowing." The first permitted banks to foster credit issuance well beyond what their strained capitalization would permit; the second used the borrowing power of the Treasury to reliquify savings banks and other mortgage lenders.

At America's top 10 banks, off-balance-sheet liabilities of \$1.5 trillion are twice as large as the banks' reported balance sheets.

The second prop has been the \$230 billion per annum issuance of mortgage guarantees by such federal agencies as the Government National Mortgage Corporation and the Federal National Mortgage Corporation.

Within a week, the Reagan administration has removed both these props—raising the prospect of the nastiest credit-deflation in American history.

As reported in this space last week, the U.S. Federal Reserve celebrated the new year with a ruling that would impose capital requirements on these "off-balance-sheet" liabilities by sometime this spring.

The President's Fiscal Year 1988 budget includes mortgage price restrictions that could drastically reduce the federally supported agencies' issuance volume. Currently, they cannot buy mortgages above \$133,250.

Under the proposed budget, FNMA and FHLMC could not handle

mortgages for homes costing more than three-quarters of the average sales price in an area. In most regions, that would bring the maximum mortgage which the government agencies might purchase to below \$100,000, and in many cases to less than \$90,000, eliminating a huge part of their potential activity.

Reagan officials say that the federal agencies "impeded the growth of private conduits" for loans. But the supposed victims, private mortgage lenders, and the savings institutions, are furious about this, predicting scarcer and more expensive mortgages.

Precisely how badly this will affect mortgage markets is hard to tell. However, the administration's sudden concern for the private mortgage lenders emerged a month after various Wall Street seers "predicted," in other words, demanded, a sharp drop in credit demand during 1987.

Federal mortgage purchases probably exceeded \$230 billion last year. Private, unguaranteed mortgage securities were sold at a \$130 billion annual rate. This is the largest element of the credit market.

Now that the federal government has postponed picking up the tab for the bankrupt Farm Credit System, and the bankruptcy of the Pension Benefit Guaranty Board has become a public issue (see Domestic Credit), Wall Street has ordered Washington to shut down the flow of credit. The bankers' concern is far from unfounded, but a sudden restriction could produce a quicker and nastier collapse of the

housing market than any other action.

EIR warned in October 1986 that rising mortgage delinquencies could bring down a trillion dollars of federal guarantees for mortgage-backed securities, issued by such agencies as the Federal National Mortgage Association, the Federal National Mortgage Corporation, the Government National Mortgage Association, and so forth.

These agencies, which put the full faith and credit of the Treasury behind securities which "pass through" mortgage payments to bondholders, cover barely 1.5% of the value of the guarantees with their own capital; mortgage delinquencies are already at a 1.07% annual rate and rising fast. Anything above the 1.5% rate will be paid by taxpayers.

Residential mortgages more than 90 days past due rose to 1.07% of all mortgages outstanding in the second quarter of 1986 from 0.91% in the same period in 1985. The rise is thus far attributable to the disaster situation in several regions, particularly in the oil-producing states, which are suffering record delinquencies.

The post-Election Day wave of mass layoffs will extend this pattern to the rest of the country, making these agencies candidates for a bail-out by the middle of 1987. Congressional investigations have shown that they have bought paper, in many cases, which is either overvalued by speculation or fraudulent to begin with.

The housing boomlet of 1985 to mid-1986 was an important feature of the Reagan administration's "economic recovery" hoax.

Now that the debt issuance attached to that hoax threatens to run out of control, and hence the "full faith and credit" of the United States is likely to be called upon, the administration has apparently decided to call the whole thing off.