Slipping and stalling with housing

By Paul McMorrow

May 13, 2011

BRUTAL SETS of housing data have been rolling in over the past couple weeks. Whether from economists or real estate firms or mortgage companies on the government dole, the numbers all point in the same direction — America's housing market is in a double-dip swoon.

If the numbers showing housing prices slumming it around their spring 2009 lows aren't troubling enough, then the surrounding context certainly is. The federal government spent trillions of dollars lifting housing — the recession's great instigator — out of its trough. And now that home prices have collapsed again, the feds have far fewer tools available to prop them up again.

By now, we're all acquainted with the link between housing prices and the larger jobs picture. A booming housing market fueled a wider economic expansion, and when the housing bubble burst it caused catastrophic damage to employment and bank balance sheets. Housing gains and losses play an outsized role in the direction of the overall economy. Housing has propelled the economy out of prior recessions, and its current dysfunction is one of the culprits behind the middling pace of the current recovery.

That's why Washington has tried so hard to prop up the housing sector.

The White House nationalized
Fannie Mae
and
Freddie Mac
, wrote the two mortgage lenders a blank check (the current total tops $140 billion), and told the two firms, which were collapsing, to increase their book of business.

The Federal Reserve, dissatisfied with the impact of giving banks buckets of free money, bought up $1.25 trillion in mortgage bonds, and then another $600 billion in US government debt, all in a bid to depress mortgage rates.

Congress passed a lucrative tax credit for homebuyers. The incentive pushed up prices and crammed a year's worth of buying and selling into last spring, but in the credit's absence, home prices have retreated to near their post-crash lows. Home prices in Massachusetts are currently off their highs by 19 percent; in Rhode Island, they're down by more than 31 percent.

It has been five years since the housing bubble peaked, and despite all that effort from the feds, prices are still bumping along the bottom. Low values portend more defaults and foreclosures. Fannie Mae is bleeding money once again. It requested another $8.5 billion from the Treasury last week, and the company warned that low housing prices would likely lead to further losses this year. One in every five of Fannie's loans is worth more than the house it's tied to. For mortgages written in 2006 or 2007, that number is one in every two.

Two years ago, when housing prices were looking ugly and dragging on the rest of the economy, the feds did everything they could to prop up prices. Washington has far fewer options for combating this second dip. The Federal Reserve's debt-buying spree is over, and not with great effect. Its last buying binge was based on the assumption that, as Fed Chairman Ben Bernanke put it, housing was "already very weak,'' and it "can't get much weaker.'' Meanwhile, Congress and the White House are haggling over steep deficit cuts, using the nation's statutory debt limit as a political wedge. Such a fiscal climate leaves Congress with little leeway to artificially prop up home sales for an indeterminate amount of time, as it did with the homebuyer tax credit.

Federal policy is, in fact, pulling in the direction of fewer home sales and lower values. A tax deduction on mortgage interest is a popular target for deficit hawks. The Obama administration has announced plans to cut the Federal

Housing Administration in half. New federal regulations will make mortgages more expensive and tougher to qualify for, driving down housing sales. Fannie and Freddie, the nationalized mortgage giants that backed 90 percent of the mortgages written in the year’s first quarter, are being driven out of business.

Still, Fannie and Freddie’s demise might not come as quickly as envisioned a few months ago. Washington policymakers badly want vengeance on the two lenders for triggering the costliest bailout of the financial crisis, but they want to prop up housing even more badly. And since their monetary and fiscal policies for propping up housing have failed, there will be tremendous temptation to crank up the old standbys one more time. Especially when the old standbys reside off the government’s own balance sheet.

Paul McMorrow is an associate editor at CommonWealth magazine. His column appears regularly in the Globe.