



EXCHANGE

Subcommittee on Capital Markets

Richard H. Baker, Chairman
Securities, Insurance, Government-Sponsored Enterprises

The News from U.S. Rep. Richard H. Baker

Sixth District, Louisiana

FOR IMMEDIATE RELEASE: August 1, 2001

CONTACT: Michael DiResto, 225-929-7711

Opening Statement

The Honorable Richard H. Baker, Chairman
House Financial Services Committee Subcommittee on
Capital Markets, Insurance and Government Sponsored Enterprises
Hearing, August 1, 2001

“Office of Federal Housing Enterprise Oversight Risk-Based Capital Rule”

Today, the Subcommittee will conduct oversight of the risk-based capital rule that the Office of Federal Housing Enterprise Oversight has recently finalized and will issue in the near future. This hearing is also being held pursuant to our responsibilities under the Congressional Review Act. I welcome our witness, Armando Falcon, OFHEO's Director.

I congratulate Director Falcon on completing this long overdue task. I have repeatedly urged OFHEO to promulgate this rule, so that OFHEO can better ensure that Fannie Mae and Freddie Mac are adequately capitalized and operating safely. This risk-based capital rule is an important step in the right direction.

In this rule, OFHEO confirms some of my long-standing concerns about market discipline and systemic risk.

To quote from the rule:

“Government sponsored enterprises are not immune to failure.”

“For most firms, debt markets provide strong capital discipline, penalizing a firm that is excessively leveraged with higher borrowing costs. That discipline is largely lacking for the Enterprises because of their status as Government sponsored enterprises.”

“The economic distress of Fannie Mae in the 1979-1985 period was significant...but for a fortuitous change in interest rates, Fannie Mae might have collapsed, costing investors or the Government billions of dollars. Because of the growth of the Enterprises, a failure today could result in much greater loss. Depending on the response of the Government to such a failure, significant disruption to the financial and housing markets, significant burdens on

taxpayers, or both would result...the Enterprises have considerably more dollar exposure than the entire savings and loan industry had in 1986.”

To the extent that market discipline of GSEs is lacking, I have offered legislation for new, stronger regulation. I remain concerned that Congress may not have constructed a regulator fully capable of getting its arms around Fannie and Freddie.

I believe the regulator of Fannie and Freddie should be more bank regulator-like. Specifically, I have looked at moving regulation of Fannie and Freddie to the Fed or the Treasury with a “Comptroller of GSEs.” Based on a GAO study, I want to give this new regulator the same supervisory and enforcement powers as federal bank regulators and also comparable financial resources to do the job. In this regard, I look forward to receiving the Administration’s views on GSE reform.

OFHEO’s risk-based capital rule is highly complex and will be the subject of considerable analysis in coming months. While I commend OFHEO for producing this rule, it is premature to say the rule will remedy all of my concerns about safety and soundness. Today’s hearing is the first of what I intend to be periodic oversight hearings on the workability of this rule and, most importantly, its effectiveness.

OFHEO lacks some of the supervisory resources available to the bank regulators for large, complex banks, yet OFHEO has chosen a risk-based capital system that is heavily dependent on its ability to field a large team of financial markets experts. I encourage OFHEO to work constructively with GSE management in this sophisticated arena.

I am particularly interested in exploring how the OFHEO rule differs from bank risk-based capital standards. For example, it is my understanding that bank regulators take a more cautious view of derivatives and limit the use of derivatives, requiring banks to hold risk-based capital regardless of how many derivatives may be in place.

In coming months, I will focus on the implementation of this new capital standard as well as any potential improvements, and, at the same time, work together with all interested parties in pursuit of broader regulatory reform, particularly an effective safety and soundness regime.