April 30, 2026

Submitted electronically via email

Ms. Agata Zhang
Secretariat
Treasury Market Practices Group

Re: Consultative Summary Note: *Theoretical Implications for Agency MBS Market Liquidity and Functioning of any Potential GSE Ownership Structure Changes*

Dear Ms. Zhang:

The Housing Policy Council[1] ("HPC") appreciates the opportunity to comment on the Treasury Market Practices Group's (the "TMPG") Consultative Summary Note: *Theoretical Implications for Agency MBS Market Liquidity and Functioning of any Potential GSE Ownership Structure Changes (*the "Note"*).*[2]

HPC and its members share TMPG's interest in a well-functioning agency mortgage-backed securities ("agency MBS") market. HPC members are leading mortgage market participants and key counterparties to Fannie Mae and Freddie Mac (the "GSEs"), producing and servicing a significant volume of the mortgage assets backing agency MBS. You correctly note that a deep and liquid agency MBS market is "vital" to our financial and housing system. U.S. homeowners benefit from the stable flow of credit facilitated by the agency MBS market, which is designed to operate in all economic conditions.

HPC has consistently advocated for a housing finance system that provides reliable access to secondary mortgage market funding sources, including predictable liquidity and fungibility in the agency MBS market constituted by the GSEs and Ginnie Mae. This market is characterized by the unique To-Be-Announced ("TBA") forward trading mechanism, which creates efficiencies and reduces costs.

TMPG's Note appropriately recognizes the potential disruptions to status quo market functioning that could arise from changes to the GSEs' governance structure. However, there are costs to maintaining the GSEs in their present conservatorships that TMPG should also consider. Policymakers

[1] The Housing Policy Council is a trade association comprised of the leading national mortgage lenders and servicers; mortgage, hazard, and title insurers; and technology and data companies. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable homeownership opportunities in support of vibrant communities and long-term wealth building for families. For more information, visit www.housingpolicycouncil.org.

[2] https://www.newyorkfed.org/medialibrary/Microsites/tmpg/files/Consultative_Note.pdf.

must weigh both the drawbacks and benefits to structural change. Maximizing policy outcomes on one axis (e.g., standardization) will entail tradeoffs elsewhere (e.g., competition). Below we highlight some of the shortcomings that stem from focusing the GSE reform discussion too narrowly on the benefits of the status quo framework.

<u>The Government "Guarantee"</u>

HPC cautions against depicting today's discrete "guarantee" mechanism – vis-à-vis the Preferred Stock Purchase Agreements ("PSPAs") – as the sole or best means to maintain the valuable market liquidity provided by the GSEs. Since the establishment of the PSPAs at the start of the conservatorships, explicit government support for the GSEs has been codified partially and temporarily at the entity-level. "Partially" because it is capped at the size of the remaining Funding Commitments under the PSPAs.[3] "Temporarily" because this capital support is contractual, not statutory, and the Treasury Secretary's authority to purchase new GSE securities expired in 2009.[4]

Open questions remain as to the durability of the PSPAs outside of conservatorship. Relying on the PSPAs as contractual commitments alone introduces uncertainty to the marketplace as to the mechanism for the government's support, which could negatively affect agency MBS.

The downside to the PSPAs and associated explicit government funding is the loss of private market discipline. Market discipline motivates private companies to operate in a commercially viable manner, engaging in competitive business activities grounded in sound financial and risk management practices. Over the course of conservatorship, the GSEs have become increasingly divorced from such market-imposed discipline in part because they have been able to access taxpayer support made possible by PSPA funding.

For the GSEs to perform their public purpose through all market conditions and maintain the confidence of the agency MBS market, some type of countercyclical funding support is likely needed. However, policymakers should consider liquidity and funding mechanisms that provide support while promoting market discipline. Legislation can institute a clear, defined, and remote role for this federal support.

Fortunately, the primary obligation of the GSEs – to provide credit risk protection to agency MBS investors to facilitate the flow of capital through the housing finance system – does not depend on the PSPAs. A healthier end state for GSE reform would preserve the GSEs' critical functions and beneficial market outcomes with alternative forms of government supervision and support. In other words, the status quo *outcome* is possible without the status quo *funding mechanism*.

<u>The Importance of Private, At-Risk Capital to a Resilient Agency MBS Market</u>

Agency MBS investors operate with an expectation that: (1) they will not face credit risk on the loans that collateralize GSE MBS, and (2) they will be returned their principal at a predictable interval in

[3] $254 billion remains available to the GSEs under the PSPA Funding Commitments ($113.9 billion for Fannie Mae and $140.2 billion for Freddie Mac). The remaining Funding Commitments cannot be increased administratively.
[4] See Pub. L. No. 110-289, § 1117 (codified at 12 U.S.C. § 1719(g) and 12 U.S.C. § 1455(l)).

the event of borrower nonpayment (e.g., GSE pass-through of principal and interest or repurchase at par of a delinquent loan). TMPG's Note correctly itemizes the cascading implications if this expectation is compromised.

These investors have a vested interest in and benefit from well-capitalized GSEs. Private capital should promote prudent risk discipline, foster price discovery, and motivate rigorous counterparty risk management that collectively reduces the prospect of government intervention – and the attendant policy risks of invoking taxpayer support.

As the TMPG note recognizes, the Federal Housing Finance Agency ("FHFA"), under its conservatorship authority, instituted key changes to address pre-conservatorship financial weakness and risk mitigation shortcomings. For example, FHFA established the Enterprise Regulatory Capital Framework ("ERCF") to improve the quality and quantity of capital the GSEs are required to hold against risk exposures. Sufficient capital should signal to agency MBS investors that the companies will be able to service their credit guarantees and facilitate new issuance even in stressed conditions.

FHFA also directed the GSEs to engage in credit risk transfer activities to shift risk to other credit markets and to put private capital in front of taxpayer support. The GSEs have transferred risk on over $7 trillion in notional single-family mortgage exposures. Credit risk transfer with meaningful attachment points (i.e., the point at which CRT investors begin absorbing losses) can provide feedback to the GSEs on their own guarantee pricing and provide advance warning where a buildup of risk might impact market stability. These market-based mechanisms complement a healthy, rates-focused agency MBS market.

In other words, the GSEs in any future state should be held accountable by their regulator for managing the credit risk they hold on the mortgages that collateralize their agency MBS. This is their primary function as private issuers – securitizing agency MBS and protecting MBS investors from credit risk. To do so, the GSEs must hold sufficient private capital against that risk and should distribute some of that risk to other market participants.

GSE reform should also establish mechanisms that allow a GSE to fail and be placed into resolution without denting agency MBS investors' confidence as to the remoteness of the credit risk embedded in these securities. Credible GSE resolution that puts private capital at risk is essential to promoting prudent risk discipline on GSE issuer behavior.

<u>Broader Regulatory Treatment of Agency MBS</u>

In addition to promoting the flow of capital for mortgage origination, agency MBS are ingrained in our financial markets as a source of funding and liquidity. For example, they serve a critical function in bank liquidity management. Under U.S. banking regulations, agency MBS are eligible for inclusion as Level 2A High-Quality Liquid Assets (HLQA) and support banks' compliance with the Liquidity Coverage Ratio (LCR) and related liquidity requirements. This favorable regulatory treatment supports agency MBS by promoting an important source of stable, structural demand from bank portfolios.

Given that banks are the largest single class of MBS investors, any changes to the GSEs' current status must weigh the broader financial system impacts from those actions that could diminish the demand for and liquidity of agency MBS. A reduction or loss of HQLA status, increased haircuts on repurchase agreements secured by agency MBS, or other actions that adversely impact demand for agency MBS are likely to have negative externalities beyond direct TBA market functioning.[5]

The broader regulatory treatment of agency MBS is an essential, but often underappreciated, component of today's highly functional market and should be explicitly considered in any evaluation of potential GSE ownership or structural reforms.

The Benefits of Competition in the Secondary Market

Today's UMBS market relies on FHFA conservator directives, regulatory requirements, and market practices to keep the GSEs functionally aligned in their policies, programs, practices, and pricing. In effect, this imposed alignment limits the ability of the GSEs to compete and innovate. Replicating this status quo outside of the conservatorships will be challenging and may be at odds with attracting private financial and human capital to the GSEs. Re-privatization of the GSEs should preserve enough standards from today to promote a liquid and resilient TBA and agency MBS market while also providing incentives for capital providers to participate and earn market returns.

TMPG's report correctly points out potential challenges to the Single Security Initiative ("SSI" or "UMBS") that could arise from multiple private, agency MBS issuers competing in the conventional conforming secondary market. However, UMBS can evolve without being abandoned. HPC believes a middle ground exists that preserves what works in the UMBS market, while allowing the GSEs greater flexibility to compete.

In the current GSE reform discourse, a *competition* argument does not get the same attention as a *preservation* argument. The housing finance system has operated for so long without a level playing field across market participants, there is understandable reticence for what *competition* could mean in access and affordability, and what it might cost. Nor can we substantiate a counterfactual for what the marketplace might have gained from greater competition had the GSEs not been in conservatorship for nearly 18 years.

Competition could bring added benefits through greater systemic stability, product innovation, operational efficiencies, and customer service that ultimately benefit homebuyers. A more competitive secondary market likely means a less aligned secondary market, but that need not be mutually exclusive with a well-functioning TBA market.

Transition Considerations for Treatment of Agency MBS

The TBA market benefits from both its depth and liquidity, as well as the broad fungibility of pools within the TBA guidelines. Changes to the GSEs could affect the fungibility of UMBS issued before

[5] For example, such outcomes could raise banks' liquidity costs, reduce balance sheet efficiency, and diminish secondary market demand for agency MBS, ultimately increasing mortgage borrowing costs for consumers and weakening overall market liquidity.

and after that change is executed. This transition will require careful attention, and potentially a bridge framework, to allow agency MBS pools to remain fungible.

Fortunately, we have recent experience from which to draw. In 2019, Freddie Mac successfully facilitated the exchange of its outstanding Participation Certificates (i.e., MBS) for UMBS. A critical takeaway from this example, and indeed the multi-year transition to UMBS, is that changes to a market of this size and interdependency require broad stakeholder participation to be successful. Quick, unilateral policy changes risk damaging TBA fungibility, with feedback into the cost of mortgage credit.

Conclusion

Preserving current market functioning associated with the agency MBS status quo and resolving the GSE conservatorships is a challenging but not an impossible task. While TMPG is correct to call attention to some of the risks associated with change, policymakers should not lose sight of the benefits to the ecosystem from transitioning away from conservatorship's reliance on government funding and blanket GSE alignment, while also preserving the market, regulatory, and liquidity attributes that underpin durable demand for agency MBS. Preserving what works in the status quo is not the same as preserving the exact framework of the status quo.