THE BROOKINGS INSTITUTION

THE FUTURE OF HOMEOWNERSHIP IN THE UNITED STATES

FEATURING BANK OF AMERICA CEO BRIAN MOYNIHAN

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P R O C E E D I N G S

MS. DYNAN: I'm Karen Dynan, Vice President and Co-Director of the Economic Studies Program at Brookings. I'm pleased to introduce our keynote speaker for today, Bank of America President and CEO Brian Moynihan. Brian has been CEO of one of the world's largest financial institutions since 2010. Bank of America serves many different audiences, consumers and businesses of all sizes, as well as institutional investors with a full range of banking, investing, asset management and other financial and other risk-management products and services. If you are thinking that you see them everywhere, you are correct. They bank in one out of two every American households.

I've gotten to know Brian through my work on Bank of America's National Community Advisory Council. The council is a group of consumer advocates, community development promoters and wonky types like me who offer thoughts to the bank on how it can best help underserved Americans. Brian grew up in a small town in Ohio, the sixth of nine children. In high school he had a job as a busboy, dug ditches for sewer projects and worked after school at a plant that made industrial magnets. He later attended Brown University, that's something we have in common, where he played rugby quite well according to my rugby plating friends, and he met his future wife. Brian took a somewhat atypical path to the top of the banking world. He is a lawyer by trade with a law degree from Notre Dame. He started out in the general counsel's office at Fleet Financial in 1993 which then merged with Bank of America in 2004 and was eventually elevated to general counsel in 2008. When Bank of America bought Merrill Lynch as it was teetering on the edge of bankruptcy during the recent financial crisis, Brian was named CEO of the investment firm and then CEO of the bank. Brian became CEO at what I think we all would agree was a tumultuous time in the banking industry. Under his leadership the bank has focused on reducing noncore assets and businesses as well as its mortgage servicing portfolio. "Fortune" magazine wrote of Brian, "A close look at his career reveals that he has proven his mettle for two decades as a deal maker, team builder and crisis manager." And he is perhaps uniquely suited for the job of chief executive in today's banking world. The business is now so complicated and so fraught with hidden dangers lodged in such esoteric products that the best leaders are those who are totally immersed in the data and details, the ones who serve as their own risk managers. That's Moynihan.

Brian is going to speak, after that he'll take questions and then we'll have a panel discussion featuring several prominent housing experts. With that, please join me in welcoming Brian Moynihan.

MR. MOYNIHAN: Thank you, Karen. As Karen said, she is a member of our National Community Advisory Council which other members of the panel are too and we appreciate the work they give us, the insight they give us and the advice they give us. I'm grateful to be here with the Brookings team for putting together this important forum.

As you think about things, there's a saying that says confidence never comes from knowing all the answers, but being open to all the questions and I think that's where we are with housing in the United States, to think not about the answers but really to focus on the questions. Forums like today are designed to challenge our thinking to tackle those questions and to raise those questions so we can get the answers. Questions about the impacts of the recession, population growth, the future prospects of that on homeownership. Questions about lending standards and how those will ensure homeownership is successful and, most importantly, sustainable for borrowers. Questions about the role of a strong, affordable rental program will play in the future of housing for our people. And questions about the proper role of the government and the private sector and the balance between those and our financing system. By focusing on these questions we can build confidence in the housing system going forward.

We obviously have a distinguished panel that you will see later that will discuss these questions and I invite all of you to keep pushing this dialogue forward to make sure that we can replicate this conversation not only today but in the coming months to ensure we reach the right outcomes. It's a dialogue that the Bank of America is committed to be a part of and one we're looking forward to having, having gotten through one of the tough periods of time in the country's housing history.

To begin this dialogue I want to make a few observations today about where we are in the housing recovery and I'll talk about some other issues. There is an incredible amount of work that has been done over the past few years to help homeowners in distress. In the last year, we and our colleagues in the industry made great progress. We've implemented the programs that the government has sponsored including the mortgage servicing settlement. You've now seen greater stability in home prices around the country, but obviously there is work to do. There are still areas of the country that are hurting more than others. The housing market is showing signs of real sustained recovery. Overall, home prices are up. Housing demand is up which means more construction which is a good thing for the overall economic recovery and for jobs. Delinquencies in the portfolios continue to decline across the industry. National standards are in place and the alternatives for foreclosure have been in full swing for many months and quarters.

Our company acquired Countrywide at the height of the housing crisis and inherited an extremely distressed portfolio. As a result, we've done a lot of work to help and assist homeowners. Today we've helped nearly 1.5 million, that's one and a half million people, avoid foreclosure through modification, short sales and other programs. Today our company has 50,000 plus people working on this, 50,000 people working with these borrowers every day. To put that in perspective, only a quarter of the Fortune 500 companies have a total of 50,000 employees and we have them dedicated to this task. The industry has put tremendous resources at work to help customers get the right solution. Modification programs offer payment relief, short sales and relocation assistance, in some cases up to $30,000. And we have principal reduction programs that are in full swing now cutting principal on average of about $150,000. These programs continue to make a difference for the customers that can be helped, but even with a strong arsenal of programs and generous principal forgiveness, redefault rates while better are still high in these programs.

Why is that true? Because at this point in the cycle it isn't a lack of programs, it's other issues causing it. Many customers still are fighting unemployment or underemployment or have become unemployed or have an unpredictable employment posture going forward. They still feel the impacts of the recession and lack the cash flow to sustain the payments, even a modified one. Important to the housing recovery is letting the process continue to move forward to help customers get the right solution even if that means transitioning to rental. To give you a sense of that, in 40 percent of all the foreclosure sales that we have today, the property is vacant, so we also must become more efficient in how we move those homes back into the system. To do that we work with cities like Chicago on an initiative to fast-track vacant properties through the foreclosure process so that we can get them useful again. Getting vacant properties back on the market as fast as possible makes a big difference in our communities and cities and to neighbors who don't want to see abandoned homes on the street. What is true today has been true throughout this. When a home is taken possession by us, we sell it within 60 to 90 days. We've also partnered with cities like Detroit and others on programs that donate and rehabilitate vacant properties. We just announced this week a partnership with Habitat for Humanity, a partnership that will donate 2,000 vacant properties, a partnership that will provide those properties and rehab those properties to people in need for an affordable home. We've also committed to donating over a thousand properties with a specific focus on returning military. So far this year we've completed about 150 donations to military families, families like U.S. Army Specialist Nicholas Salerno and his fiancée and two children who recently received one of our donated homes in Tampa. Specialist Salerno suffered serious injury in his last tour of duty in Afghanistan. He and his fiancée have credited their new home with providing the fresh start that their family needed.

As we think about housing and the future of housing, how does everything we've learned during the crisis and recovery apply? It underscores the need to shape a system that keeps borrowers out of the situation of owning a home and not being able to afford it. It means shifting the conversation from what percentage of Americans own homes to what is the right solution at the right time for every individual customer. As the housing market strengthens, now is the time to have this dialogue in earnest so that we can reset to a more secure, more sustainable system for all the players involved.

What I'd like to do is frame the rest of my remarks around the main participants in our housing system, homeowners and homebuyers, lenders and the government. I want to discuss some of the assumptions we need to challenge and discuss the questions we need to ask in terms of what a reset might look like. Let's talk about the reset. For homeowners, what are the resets that we have to make around homeownership? What is remarkable is given everything that people have been through in the past several years, survey after survey continues to show that the overwhelming majority of Americans still aspire to homeownership. Most Americans still rank homeownership as an important part of their view of the American Dream. But as you look deeper into those surveys, you'll see that much of the value that Americans place on owning a home is emotional and not financial. Take for example the most recent Fannie Mae housing survey. The top two reasons for homeownership were to have a good place to raise children and a safe place to live. As a just democratic society, we all are citizens of a safe, good place to life, but a roof over one's head doesn't always have to come with a mortgage and in some cases it shouldn't come with that. Homeownership is valuable. There is no question. It stabilizes the community and leads to more civic engagement and investment. Those things have been proven over time. For those who purchase a home for a place to live and make long-term payments, a home can also provide a vehicle for wealth creation. It's important to recognize that much of the value created during the housing bubble in the mid-2000s was more the result of expanding credit and not overborrowing and overlending than it was from underlying home value appreciation on the fundamentals. Think about it. Historically, long-term average of home appreciation going back to 1975 is 4.6 percent and that includes the recent bubble and burst years. Since 2001, the average appreciation has been 2 percent. So leading up to the crisis, the virtues of homeownership, stability, security and savings, got disconnected in the 2000s from the act of homeownership. The laudable goals of an ownership society evolved from building long-term equity to cashing in on short-term gains. In many cases it became less about a safe place to live and more about making profits. Home purchases for investment gains and not for shelter increased from an historical average of about 4 percent to 28 percent in 2006. Homeowners have -- and their home became the norm. Cash out refinances, using the money for other things other than improving the home or developing the home completely disconnected the positive aspects of owning a home from its value. According to a Freddie Mac report, for eight consecutive quarters at the height of the crisis in 2005 -- the buildup in 2005, the cash out refinances exceeded 80 percent of all the refinancing. So a question that we need to consider and policymakers need to consider is that it people are going to take cash out of their home or speculate on their home and buy for investment or buy properties to rent as an investment should they be able to do so with mortgage capital, especially mortgage capital that is guaranteed by the government. We need to look hard at some of these old assumptions and ask the question if homeownership is the right solution for everyone. Are there more valuable and flexing housing options? We also have to challenge the assumption of stability versus mobility and other factors that impact two-income households, changes in family structure, all the things that have become a part of our modern society. Workforce mobility and flexibility is increasingly important to people in America to counter potential income shocks, locational decisions about where to work, and as was the case in the last recession, has been the case up until today. According to some of Karen's research that she's found, the volatility of household income rose nearly 30 percent in the past four decades. In addition to these realties, the past 5 years of high unemployment and underwater home values have taught us that sometimes flexibility for workers and people to move and not being burdened by a mortgage is a virtue. A 30-year mortgage contract does not provide flexibility in some cases. So we have to challenge the assumptions about the flexibility and mobility of the American people relative to housing and mortgage finance.

We also have the challenge the assumptions about the purchase cycle. It's important to understand that the purchase cycle, the cycle over which you buy homes, has fundamentally changed. Macro conditions were working in favor of a robust housing market. The economy was strong. Population growth was high. Demand continued and high house prices continued to rise. A lot of that isn't so true anymore. The world looks at the United States and the United States looks at itself with a fundamentally projection of growth. If we were sitting in this room in 2003, the forecasters would have expected a growth rate of 1.3 percent in GDP for the next 6 years ahead and a long-term average over sustained decades ahead of 3.3 percent. In 2012 those forecasters who are sitting here today would say they expect 1-2/2 percent growth for the next 6 years and a long-run average of 2.7 percent. Along with lower expected growth, unemployment is more uncertain and long-term unemployment has risen to record levels. Today 40 percent of unemployed workers are employed for longer than 6 months. That duration is at historical levels. The historical average is 13 percent. That again affects people's stability in times of unemployment in their ability to make their mortgage payments. There is also the issue of what is the probability of unemployment? Is it higher now than it used to be? I think statistics would prove that true. U.S. household formation has also slowed dramatically. Average annual household growth over the last 5 years has been about a half-million a year, less than half the pace in the first part of the 2000s. And if you look regionally, and housing is always local, the demographic issues we just described are much different by different areas of the country. In cities like Detroit there's a substantial population in the past decade according to the census that the debate about homeownership is much different in a city like Dallas where population growth has maintained it strength.

All of these factors taken together, weaker economic growth, slower household formation, employment uncertainty, duration of employment uncertainty all make the purchase cycle or should make the purchase cycle slower and it will make it harder for a borrower to find an escape valve if they end up with a mortgage that becomes unaffordable for any issues at any time. Another thing we have to challenge is the assumption about risk. Ultimately we believe a more sustainable housing model rests on more than just prudent lending standards, but also on our ability to educate America about the inherent risks that come with the responsibility of homeownership. At Bank of America we continue to focus on homebuyer education and partner with a network of more than 600 nonprofits to provide purchase counseling in connection with mortgages. Coming out of the crisis, credit repair will also be a prime focus and we're working with counselors and educators on steps that consumers can take to repair their credit and prepare for sustainable homeownership going forward. Absolutely homeownership is important and the American Dream is important, but when you think about and understand the real attributes of homeownership as we look forward, then we have to understand the risks. Even a responsible home-buying decision carries some risk. I get letters every day from our customers. Customers are struggling to pay their mortgages. If you want to read those letters, they tear your heart out. These letters are from people who can't pay their mortgages for the same reasons they couldn't a decade ago or two decades ago or three decades ago when I started in this business. They've gotten sick. They've gotten divorced. They've lost their job. They've lost their income levels.

Uncertainty is not going to change as we look forward. So as we think about these questions from the homeowner's side, there are the kinds of issues that we need to reset.

How do we support the positive aspects of homeownership? How do we help make people make smart financial decisions that are not based on assumptions which may not be true in the decades ahead? How do we promote the benefits of homeownership while preparing people for the risks and responsibilities that come with it? That's on the homeowner. Now let's switch to lenders like ourselves.

What are the resets that we need? Here the discussion often becomes centered on the availability of credit, whether banks should simply be lending more. Let's take a step back. By being overly aggressive, the entire housing system caused a great deal of damage to the very people we were trying to help with homeownership and that damage was certainly not caused because we weren't lending enough. In fact, we were lending too much. The U.S. mortgage crisis originated with a dramatic expansion of credit. Lenders prompted by lower interest rates, rapidly rising home prices, large amounts of investment capital made credit available to borrowers who previously would not have qualified or at levels they would not have qualified for and that ultimately proved to be unsustainable. Subprime loans, little or no down payments, all the things we now know a lot about expanded dramatically. At Bank of America our primary window on this was through our acquisition of Countrywide. We exited subprime lending in our company's history in 2001. In fact, we were criticized by some for not being in subprime lending and that was fine with us. We did so and still met our longstanding commitment to make loans for low- and moderate-income buyers and at the same time we did not participate in subprime. There is no doubt that post-crisis credit is tighter, but there is also no doubt that a fundamental part of the lending reset has been reinstituting high-quality underwriting, eliminating specifically designed programs that no longer apply. But if you think about what the industry has been through and what our country has been through and what our customers have been through, there can be no margin for error as we look ahead. We have to make sure that the asset that we originate, the loan that we originate, is ironclad. That's not bad. It just takes a lot more time than it used to. But credit is available. We've extended more than $53 billion of mortgage lending this year to nearly 215,000 borrowers. Thirty percent of these loans have been made to low- and moderate-income borrowers. The industry has originated about a trillion-three so far this year. Access and availability of credit are critical and lenders have reset along tighter standards and there are opportunities that may exist for some more flexibility. But we can't go back to where we started. We can't go back to where we were.

Do we believe homeownership is a good to be pursued at all costs? If we don't believe that, and I don't think any of us do, then strong underwriting and quality credit standards are our best protections against putting people in homes that they can't afford and that's good for both lenders and for borrowers. There has been a lot of debate about down payments and there's a lot of debate going on in various groups about how big they should be, et cetera. When we think about that, a 20-percent down payment is light years from what was going on before. But think about the implications. I have a 21-year-old child. Think about and $100,000 home and saving $20,000 in after-tax proceeds from his income. How long will it take him to save that? That is an implication. Is there any magic to a 20-percent down payment? I'm not sure there is. Is 10 percent more reasonable? Maybe. It can't go back to zero because that doesn't work and we've known that. So a down payment sends positive traits of homeownership, saving, delayed gratification of having worked hard for something plus some security that you have some equity in your home if you're hit with an unforeseen event. But there are also very real concerns, and we agree with those, that too high a standard can lock people out of homeownership, something we clearly don't want as an industry and as a country. All the right voices are engaged to ensure that we land somewhere reasonable that promotes a more sustainable system and protects the homeowner. These are questions we need to think about for lenders. First, how do we make credit available but protect people from taking on too much credit and ending up in a home they can't afford? Second, how do we strike the right balance between prudent underwriting, responsible down payments and access to homeownership? Then we move to the third principle that I talked about earlier, the government. What are the resets for our government? This area of discussion often becomes dominated by the GSE reform and the stated need to by many to wind down Fannie and Freddie, but let's take a step back. Why is government involved in the housing market in the first place? There are two core reasons that we believe the government has been involved. First, to expand liquidity to provide capital and, second, by doing that to make homeownership more accessible to those who might otherwise be unable to obtain it. But currently our government role looks very different. The government dominates the entire housing finance market, as many know, backing about nine of 10 loans. FHA has been instrumental in sustaining the market for the past few years, but they've come a long way from their traditional role that they played. Their original focus was low- and moderate-income borrowers in the wake of the Depression and GIs were returning from World War II. Today they account for 20 percent of the market and prove low down payment lending for loans up to $729,000. This is an example where we potentially need a reset over time. Fannie and Freddie help continue to maintain liquidity in the market in the wake of the housing crisis and the uncertainty surrounding the market in today's real world. But we do need to move to a plan from a market dominated by the GSEs and by FHA and other government sources to one that does three things. First, we need to return FHA back to its core purpose of helping low- to moderate-income buyers. Second, the GSEs need to undertake an orderly transition to facilitate the return of private capital and that they provide clarity to the market about what credit and servicing risks they are willing to take. Third, we need private capital to come back into the market. We can do that by removing some of the uncertainties about the rules which hopefully will take place over the next year as we work forward with the remediation of the crisis.

I don't think changing any of this abruptly is wise policy. It will take time to work through all of this. We can't eliminate Fannie or Freddie without having something to absorb it so that the markets are only going to come back in on the private side when asset prices are certain which we're starting to see and if there are guarantees of liquidity for certain investors. All of these players are critical to the transition. A healthy market needs private capital so that the government and the taxpayer don't take the risk. Clearly we need that. And that market should come back in a way focused on a value exchange between the borrower, lender and investor where everyone understands the deal they are making. That's what got lost as we ran up to the housing crisis and that's what we need to restore. So we have a lot of rules that are going on with a lot of names for different things, QM, QRM, Basel III and many other names and many other rules. It is our ultimate goal to get this settled as a participant in the market and get clarity and then we can get the market reset. There has been a lot of great dialogue around these attributes and I'm optimistic that the final rule will strike a balance between consumer protection and access to credit. But we always have to be careful with all of these policy inputs into the system to make sure we work on this in an holistic way. What we don't want to end up with is unintended consequences. The phase be careful what you wish for often comes into my mind when I think about all these rules and the changes going on. We can't have private capital closed out and we can't have government dependency on the future of the housing market finance continue. These are questions that we need to consider in the reset of the government's role. How do we provide a place for government financing that stays true to the mission of liquidity and access to credit? How do we incent the return of private capital to foster more competition to shoulder the risk that now falls squarely on the American taxpayer and should not?

Let me conclude and then take some questions from Karen and you. There have been a lot of recriminations over the past few years and we believe it's time to reset, to move past the recriminations and move forward toward solutions. The chance to put the lessons learned to good use, put our housing finance system on a more sustainable path is a chance and challenge the truths of the old paradigms and reestablish them as we go forward. To reshape our finance system to provide clarity and understanding of risk. It's now our duty to provide a path to homeownership that once achieved what it always meant to be, a place to live, a place that is a reward for hard work and sacrifice, a place to put down roots, a place to have a family. Now is our chance to bring that American Dream home and it's time to reset and do that. Thank you.

MS. DYNAN: I'm going to start by thanking you. You raised a lot of themes that we were hoping to cover as we at Brookings were putting together this event. I think the questions that you raised about government policy in the last section set us up with the panel discussion that we're going to have in a few minutes.

Let me start with where you started with the foreclosure crisis. You said the bank is currently working on 900,000 delinquent loans. I was wondering if in this case the easiest cases have been working out such that going forward you aren't going to be able to find arrangements that keep as many folks in their homes. As a follow-up, what kinds of solutions are you offering for homeowners in cases where the mortgage doesn't appear to be sustainable even with a generous modification?

MR. MOYNIHAN: On the first issue, remember we talk about at Bank of America how we had a million-six seriously delinquent mortgage loans at the peak and now we're down to 930,000 in 2012, but remember it's not the same people. You had all the new entrants to delinquency that have been going through so that in the pool of loans we have today, there are people who became delinquent 60 days or more last month and then the months before that. We're not through the programs. We still modify 30- to 40,000 mortgages a quarter, 20,000 short sales, so the amount that's going through is for lack of a better term is new dialogue, new consumers into the process. The overall levels are coming down, but the actual people in the process are new to the process so that there is plenty of relief left for people.

When we talk about the programs going forward, all the programs continue along and you see that -- reduction programs in the national mortgage settlement which are offered to a group of customers and we've made that offer and we'll finish that up, but the modifications, payments and things and programs will continue on past that.

MS. DYNAN: Do you have a sense of how long it's going to take ultimately?

MR. MOYNIHAN: As we look out, the rate of reduction is about 75- to 100,000 a quarter so that if you think about the level where we'll end up based on the portfolio of our seize might be a couple of hundred-thousand so that we've got to knock it down. As you look across the next 2 years, you'll probably see that return more to normal.

MS. DYNAN: I know you suggested that we have no shortage of programs to try to tackle these problems and I presume you were partly referring to government programs. Is there anything else you think the government can be doing to get us through the foreclosure crisis?

MR. MOYNIHAN: I think that the number one thing is that people divorce the foreclosure crisis from the economics. The reason why people can't pay their mortgage loans is generally they're underemployed or unemployed or a two income household lost earning power, people get sick and other things happen which are tragic. That has been a constant. That's gone on and shows up over time. It's the unique things such as the amount of people unemployed so I think that the number one thing is to get people back to work. The good news about that on the housing start side is you're seeing meaningful pick-up in housing construction which is one of the most stubborn places to get Americans back to and that's good news. Now we have to be careful not to overshoot again, and I can get into a great debate with some of your developer clients about what that level should be, but let's assume that we've still got room to go before we get there. I think that's the number thing, we got to get people back to work.

The programs are there, if the investors will come along, we still need more participation in more investor groups and that will provide more fuel. If the economy continues to improve and we see the economy continuing to improve 1 to 2 percentage points, you're absorbing jobs, creating enough jobs and things are getting better, and that's why you're seeing housing prices stabilize. Are there pockets that are very difficult still, yes, but overall the thing is getting better. I think honestly it's time now and Americans are patient and we'd all like this to be behind us and something else to be here. But the reality is with time this is working through but unfortunately it's been 6 years since housing prices quit going up and we're impatient as a society and that's because we're creative and an entrepreneurial society, but I think with time this will clear so that I'm not sure fixing it or more programs help. I think getting through the ones we have would help.

MS. DYNAN: As someone making policy recommendations, counseling patients as a policy solution -- I sympathize with that.

MR. MOYNIHAN: It's not inconsistent with the urge to fix things, but I think seriously if you watch the day-to-day progress, we've come over the top and we're coming down and we are representative of the industry, this will get done and the key is to do it right for the consumer in an empathetic, clear way, but adding more to it lengthens the process at this point.

MS. DYNAN: May I turn to a somewhat different topic which is credit availability? You made it clear in the speech that we can't go back to the kind of go-go days of lending that we saw in the middle of the last decade. I completely agree with that. But speaking of things overshooting, we saw the credit availability pendulum swing too far in the other direction during the financial crisis and subsequently we've seen credit availability get better for some types of loans as the economy has gotten better. But my sense is and this is looking at the national data that we haven't seen that much improvement in credit availability when it comes to mortgages for home purchase and that's at least for the nation as a whole. I was wondering is that true for the bank and if so can you help us understand why?

MR. MOYNIHAN: There is no question that if you think about the mortgage market as having a constant level, put on top of that was a lot of activity which is gone and should be gone. There always was a large portion of the mortgage market that went through a very standard so to speak underwriting process and then you had new programs sprung up the pace of mortgages and ease in refinancing and so that's why you had the annual turn. If you take the percentage of mortgages that were refunded in a year, you had reached 30 to 40 percent and that was because of these programs. It's come back down to really low at about 13 percent and should probably be at 15 to 20 percent so it's a little lower. The programs are there and I think the process is slow, but if you think about it from the effect on the lending community, we made mortgage loans in 2004 where people said make a mortgage loan and I want it and in 2012 they're saying I didn't want it. You're saying, wait a second. I can't take the risk that you're going to say I don't want it later so these things are going to be buttoned up and we quality control the process three times and our error rate is very low because we have to protect the integrity of the assets for periods of time which are way beyond anybody's imagination based on other people's views of what went wrong 10 years down the road looking backward. I don't think this is going to change honestly, but it's not inherently a bad thing. Then the question is is money available on low and moderate programs? As I said, we still do about 20 some program of our originations in those programs. Is money available in FHA who has made programs available for first time homebuyers and low down payments? We got to be careful about how much we can do with that, but the programs are there. Oddly enough, the biggest impact to customers, probably the more standard underwriting customer has gone from a very simple process to a complex process because we can't differentiate higher credit quality on some and that's the frustrating part of the American consumer. And by the way, it's frustrating to me because we can't get our loans closed fast enough for our customers and we've added 5,000 people on a base of -- over the last 12 to 18 months into our mortgage origination process to increase our ability to do mortgages and we're still not doing as well as we should so that it's really underwriting applied to the more traditional mortgages. I'm not sure it's time to pull back on that.

MS. DYNAN: Picking up on that last thought, I understand the reasons for that. I suspect credit availability is part of what's behind the weak household formation that you mentioned, although I completely agree that the underlying economic conditions, high joblessness, is certainly a major force there. Do you feel this is a kind of real normal or is this something that's going to change as the economy gets better?

MR. MOYNIHAN: One of the things is one of your colleagues and I had a conversation a while back, and your team has led on this, is to almost go city by city, geography by geography, and look at population trends and look at the prospects for population trends and then think about housing policy and connect. I think that's the right answer this is not an aggregate America question. It is a very different question. In the last couple of days I had all of our market presidents in from 140 markets around America and Dallas doesn't know what Detroit is taking about. They really don't. The population, Houston and the impacts -- it's just now in their thought process to think that they have a problem with unemployment or housing. Detroit, Columbia and other places have it. Parts of Massachusetts have it and other parts of Massachusetts don't. Parts of New York have it and other parts don't. So I think this has got to be very localized and figure out how you solve the question specifically. I think the availability of credit is fine. I think it's going to be tight more until we get the rules figured out and then I think you'll bring in the private capital that will help. I'm not sure that's altogether a bad thing, but I think as we plan the policy going forward we got a lot more granular by city to figure out what the right answer should be as opposed to trying to -- by community or by state or by something to figure out what the answer should be.

MS. DYNAN: May I turn down to the customer relationship and how it's changing in response to the very dramatic developments in the bank environment over the last several years? First of all, I was delighted to hear about your efforts regarding homebuyer education. It's a huge lesson from the past few years that people need to understand what they're getting into when they make this enormous commitment. Let me ask you about a different change in the customer relationship or at least a different potential change. It was reported a couple of weeks ago in one news article that I saw that the bank was backing off of a plan to impose new fees on checking accounts under certain circumstances. I'm curious. Was the report right and what should we make of it?

MR. MOYNIHAN: I'm not sure I read it. Let me tell you what we do because it's an important thing. If you think about we think of our general retail business which is a big business in America. We have about 30 million checking account holders, so we have a big business. So starting a number of years ago in 2009 I think it was we started looking at the combination of the economy and people's behavior and the new devices and everything changed things and we started thinking about that. We figured out that we had to figure out a different way to relate especially to Americans who are medium income earners and less as the way to provide services that was fair to them and fair to our shareholders and that requires change in the thought process. So we dropped the overdraft fee, for example, on debit cards in 2009 way ahead of the industry. We went to more transparency. We have lowered that. We have been managing that dialogue trying to figure out the right way to handle it. Then entered the smart phone which changes this dynamic dramatically because now you have a device that's ubiquitous and usable and available for low cost and so we're seeing that as an interesting thing and we're seeing customer behavior change as an interesting thing. We're trying to develop programs that help people have great access to banking services. Bank of America provides 5,400 branches, 17,000 ATMs, et cetera. At the same time to do it in a way that we can afford to provide a great service to them with the realities of how much revenue is available especially in this industry environment so that we started redesigning programs and we kept doing that. There's a lot of talk about what we're doing or not doing. I can tell you what we're doing. We have a great transaction platform for the core America. We have kept the prices down, we've lowered the penalty fee aspects and what we're looking for is what the model that will serve customers going forward. What we're seeing is 70,000 new mobile banking customers a week. Think about that. A half a million checks get deposited by people taking pictures of them now and we -- this product in August. So the behavior is changing so fast that I think the 20 million texts that go out to our customers every month saying your balance is low, make sure you don't overdraft, and all that put together is a tremendous level to serve customers traditionally with branches and ATMs and things like that, it was a higher cost and now you can lower the cost and therefore you can provide better services and you don't have to charge the penalty fees and that's what we're working on.

MS. DYNAN: We have time now for a few questions from the audience. I would ask you to first of all state who you are and who you're with and then also if you could keep your question concise so that we can get to as many questions as possible. With that, I think I have someone walking about with microphones. Is that right? Why don't we take this question right here in the first row?

SPEAKER: My name is -- and I'm with the National Associations of Hispanic Real Estate Professionals. You indicated in your presentation or implied that a big part of the foreclosure problem was that many borrowers could not afford the loans they obtained. According to "The Wall Street Journal," at the peak of the housing boom as many as 60 percent or more of the borrowers actually qualified for prime loans, that is, loans they could have afforded. Part of my question is what are we going to do to prevent that from occurring? Last year according to the Census Bureau there was a net increase of about 200,000 new owner occupied households 80 percent of which went to Hispanic homeowners and other minorities. At the same time, there was a net decrease of thousands of units, hundreds of thousands of units, for other population groups including whites. What are the implications to the Bank of America of these demographic changes and developments?

MR. MOYNIHAN: We have for at least a decade and maybe more, we look at our customers and we're customer driven and reflect the customers. Think about us in Los Angeles or Chicago or Houston. As customer demographics change, our ability to provide services changes so that we have branches in 10 languages are spoken, we have counseling in multiple languages to help people. So I think from adapting to the population of America and what it looks like, we've been a leader in trying to continue ways to make the dialogue with customers more native to them for lack of a better term and that's difficult. I think when you go to housing, the groups that you represent are obviously fast growing in the household population so the half-million households will have a high percentage of the Hispanic community which is great. It's a population of America and that's what makes America terrific. So serving them I don't think is that different than serving four decades ago in a different group of populations going past so that we need to serve them well.

I think when you get into the debate about foreclosures now is one that is really multifaceted, there are many things about that, which is without a decision point, without that coming to you, you can't get the dialogue going about what to do to resolve things. We have many, many events. We invite thousands of customers and about 3 percent show up because there isn't the decision point. So it doesn't always end up in foreclosure but the decision that something has to happen ends up with restructuring the loan and modification so that this is wild. But the reality is we only have about 20,000 properties that are actually in OREO (?) status in any given month, and by the way, they almost roll over. We have 900,000 people that are at some stage of uncertainty around this and only a small part and when we get those properties they're sold so how do reposition those houses and eat up that 900,000 is really a tough challenge and that's what we've been working on. We work with all kinds of community groups around the country. We've been trying to enlist them to help us because the comfort that you give your constituencies helps us have a real dialogue about what are the issues, what do we need to work through, how do we get through it, and believe me, we need everybody's help here because the borrowers have to trust the process and the system. I don't know if that answers all your questions, but that's how we think about it.

MS. DYNAN: Let's go the back.

SPEAKER: -- with the Consumer Federal -- American First. Thank you for your thoughtful overview on the housing market. It was very helpful. I wanted to ask on the point about what is the right market share for government ensured mortgages, if you look at the data on Fannie and Freddie's share of mortgage backed securities, it's pretty much within the historical range going all the way back to 1990, number one. Number two, FHA has been in a huge expansion.
And three, there is virtually no securities activity outside of the footprint of the GSEs -- in the private sector debate on influence. Given those facts, what would you say is the right percentage of the market that FHA and the GSEs in whatever form they emerge should play in the market? What's that right balance if they're currently, at least the GSEs, pretty much where they've been since 1990?

MR. MOYNIHAN: There is a philosophical question that if you can get private capital to do it all, would you want to have private capital and have the government capital applied to some other issue that we need to solve in America, infrastructure? Conceptually you'd like it. The practical reality is that if you think about the mortgage debt outstanding at $10 or $11 trillion or something like that, mortgage debt outstanding I think is 10.5 or something like that, pick a number like that, and you think about all of the deposits in the financial services system, it's about that number so you cannot finance this through the banks. By the way, the nature of the asset is such that banks can't hold it very easily. But then you have the investment community and the U.S. behind it and you have about 10 or 15 percent foreign ownership, percentage of the GSEs, so I think in the near term there is no practical solution other than to continue to participate in the governments because the reality is that with the uncertainty about home values, uncertainty about the process, uncertainty about what the asset for lack of a better term is, do you think people who don't know America or outside America could actually invest and we need their liquidity to provide the financing, the balance sheet for lack of a better term, but I think long term the private label market will be there. We shouldn't equate what went wrong with the private label market around the CEOs. It had nothing to do with the private label securities market. It had to do with the restructuring of and financial engineering around those things, but the actual underlying pass through notes and things like that that have been going for I guess almost 30 years almost now since the -- and stuff like that are there, they're true, investors want them, both U.S. and others and I think you can get there. That would require high down payment, sustainability and more sort of for lack of a better term tried and true underwriting. So the question in my mind is I think you need to bring the government down, I think you need to bring the private label up from the current level of 9 to 10 down dramatically. I think it will go away maybe, but I think that's a decade or two transition and not a 5 year transition because the amount of investment capital to sustain the level of debt in housing in America is not going to come without liquidity and guarantees. I don't want to say a certain percentage because people might imply and try to draw a line and get there, but clearly the goal should be the least amount of support you need for the goal you want and I think the goal is different now with more stable population growth in the United States that in an economy that needs to diversify a bit away from depending on housing for growth which was going on in the mid-2000s, you kind of got it where you want it so let's let it ease out. So I think they should come down to a very small amount. The question is how and when.

MS. DYNAN: I know you need to run to a different meeting so I'm going to take the last question as a follow-up which is I see your point that an abrupt change right now in the housing finance system would be a bad thing given how fragile the economic recovery is right now. We're not even really talking about what the new system is going to be looking at. That doesn't mean we have to go to the new system right now, but we're not even putting the framework out there. Is that a problem for you guys? Does it make it harder to do your business to devise the strategy that you have for lending?

MR. MOYNIHAN: I'd separate that into a couple of things. I think if we can get with the CFPB with Director Cordray and others in the QRM, QM, if you look at all these things, everybody has had their perfect answer and it's a whole bunch of things. If we can get that rationalized to a serious of things that you're done with, that provides the stability that I think at a various point you will start to see an ability to form private market capital coming back in so that I think that is the near term problem. Longer term, Secretary Geithner put out a proposal 12 months ago or 18 months ago. There have been proposals. I think it's lost behind the fiscal cliff and all the other issues at the moment and should be honestly. But I think if anything, the near term need is to finish the discussion around the core aspects of Dodd-Frank and the other rules and get that done. When you get that done and have that balanced, you can have that viewpoint, then I think it is time to have the discussion but a lot of discussion has to be how do you accomplish transition more than it does the endpoint. Frankly, a lot of debate around the endpoint's variations on a narrow scheme of the government being an insurer of way out tail risk for a reasonable price and have private markets coming in and people can have a definition of that. It's a little bit like every other debate. The answer is not that different from various constituents. The question is between here and there how do you make the transition. I think near term we need clarity on these relatively straightforward set of topics, it's not a straightforward set of outcomes, and longer term we need to come up with a policy. I think it's a 3 or 4 year discussion to get it right, potentially 2013, 2014 or 2015 and then you start to implement it but you're going to have to give lots of warning to America and lots of warnings to the market to do this right because you can't change this overnight because you don't want confidence to go backwards because of this even though your change may be less of an implication. So the debate around mortgage interest deduction, if you change that overnight and people aren't expect it, the outcome may be far more serious than the actual outcome of the change. We don't know. But part of it is to let this thing ease into the psychology of the American buyer and let people adjust their viewpoints.

MS. DYNAN: I think that sets us up nicely for the panel that comes because I think they're going to be grappling with a lot of these issues about what the new system is going to look at. Before you leave I want to say to folks that Brian is going to leave and then we are going to have the panelists hop up onstage in about 60 seconds, so we if we could get you to stay in your seats while that happens that would be terrific. Then of course before we even do that I want to thank you, Brian. I know you have an incredibly busy schedule and we appreciate you coming here to spend some time with us and tell us about what's going on with the bank.

MR. MOYNIHAN: I appreciate you sponsoring this discussion and there is nothing more important for America to get this right over time, and thank you for your participation.

MS. OLICK: Welcome on behalf of all the panelists here. I want to thank the Brookings Institution for having us here and to discuss what I believe at least is one of the most important issues in the economy going forward. I'm Diana Olick from CNBC. I cover real estate, that's all I do and that's mostly what all of these panelists talk about. We're going to give them each a chance to do a short presentation before I ask some questions and then we'll give the audience a chance to ask some questions. We're going to start with this side with Douglas Holtz-Eakin.

MR. HOLTZ-EAKIN: Thank you. Thanks for the chance to be here today. The topic is what's the future for homeownership and there are really two answers to that, what will be the future and what should be the future.

In terms of what will be the future, I want to echo something that Brian Moynihan emphasized which is the pace of economic growth in the United States. I think that's fundamental to the degree to which we quickly recover in housing markets across the country. I've been to a variety of different markets for events to look at this, Sacramento, Las Vegas, Phoenix, Orlando, Columbus, and the nature of the recoveries differs greatly, but the pattern that emerges is one in which the broader based economies recover better than those which are narrow and the importance of economic growth cannot be overstated. The second one which doesn't get talked about as much but which I think is very important is the future of U.S. immigration policy which is central to so many things and is one of the underserved policy topics in the United States. The native born population of the U.S. doesn't have replacement fertility rates so all future population growth depends on what we choose for immigration, and given the importance of demographics to housing markets, this is the issue over the longer term so that those two things strike me as central to how it will play out.

In terms of the things that we ought to do, it seems to me that we have a couple of things. The first is to recognize that it is time to look forward. This crisis began years ago now and I was once in the camp of designing very clever policies, I promise you they were very clever, solve all these problems, but more policy innovation, more new programs, more interventions I think is now beginning to make it too difficult to figure out what the rules are and to move forward. It's time to let markets clear and move forward as fast as we can. That's point number one.

Point number two is to recognize that we are determining the future of housing policy right now whether we know it or not. The example I'd point out is the QM, QRM and the Basel III accords and their implementation. Some work I've done with some others at the American Action Forum suggests that if you look at the credit implications of those rules versus normal lending say circa 2001, take the bubble years out of it, we are on track to provide financing for about 20 percent fewer mortgages than we would have had we had the standards of 2001. We ought to decide whether we want that or not because it's happening right now as we go forward. The final things which are the big ones like what are we going to do, the central focus needs to be on providing shelter for Americans and to have a clear objective of having those who are in need of shelter have opportunities to have it whether it's owner versus rent, we shouldn't have a big stake in that.

On the homeownership side, I believe there are two things that politically will end up being true. Number one, Americans will not give up their deep love of the 30 year fixed rate mortgage. Maybe second behind children, but they love it very, very much. That will require government backstop and the design of that government backstop is going to be very important. We know that the GSE model is broken and we have to come up with something different and we can come back and probably talk about that. The second and open question will be whether there has to be a front end subsidy of the type that's been the mortgage interest deduction. It may turn out that that's true particularly in a weak economy and housing market and if so I would simply implore our policymakers to not subsidize in an open-ended fashion. Our federal government is not in the position to provide open-ended subsidies for anything anymore and in particular not toward those who become heavily indebted. Let's have something that rewards equity investment in a comparable fashion. I think that's briefly the lay of the land both now and for years to come.

MS. BOWDLER: My name is Janis Bowdler. I oversee economic policy at the National Council of La Rasa which for those of you that aren't familiar is the nation's largest Hispanic civil rights organization. In my brief opening comments I want to make three quick points.

One is that demographics in this country are changing and that has huge implications for our housing policy but also our service and our programs in this space. My second point is that those borrowers don't just look different, they're not just different ages, they have dramatically different credit profiles than what we've seen in earlier generations. My third point is that we know how to do sustainable homeownership right, we just haven't focused a lot of time and attention to bringing that to scale. Let me quickly touch on each of these three issues.

The demographics issue already came up, thank you my friend Alejandro here in the front, during Q and A, but let me put a fine point on this. According to recent research, 70 percent of household growth over the next few decades is going to be driven by households of color and by 2020 half of all first time homebuyers will be Latino. That is significant. Right now babies born in this country are born into a cohort where no one ethnicity dominates so that we are seeing a dramatic shift in our population. That means that as housers we need to think about what do those communities need both on the rental side and the homeownership side and if our systems can't accommodate that, then we're going to end up with lopsided policy once again.

On the profiles, again very different profiles. We have to think about meeting these households where they're at. We've just been through a recession that has hit communities of color particularly hard. Latino families have seen double-digit unemployment for a couple of years now. When you couple that with foreclosures and the decline wealth, in fact, Latino families lost two-thirds of their wealth due to decline in home values or outright home loss. That is an extremely different profile, thinking about what they're going to need when they reenter the market looking for a home. But not just families who've had it tough. If we think about where our students are, we don't always talk about student debt in our housing conversations but we should. I saw a "Business Week" report that student loan debt is going up $3,000 a second. These are our future homebuyers. They are overleveraged already and coming into an economy where wages are flat. What their credit profiles look like again are going to be extremely different, and we can make a choice when it comes to housing policy. Do we shrink the market or do we think creatively about how to make sure that these kinds of borrowers that have very different profiles can be accommodated?

That brings me to my last point which is sustainable homeownership. For so long over the last couple of years our conversations around housing policy have been dominated by the responsible borrower. Please note my heavy use of quotes there. We talk about making sure that only responsible borrowers are able to get a loan modification or get a mortgage, but in fact we're asking the wrong question. First of all, that question implies that the run-up to the crisis and everything that went wrong we can debate the causes and consequences later and probably until we're blue in the face, but it implies a very simplistic answer to the crisis that somehow bad decision making on the part of millions of borrowers brought us here. That ignores the systemic issues that we were dealing with and makes that a much more simplistic answer than what we know is a very complex situation.

The right question for us to be asking is how do we take those models of sustainable homeownership and get them to scale so that we can build the most inclusive market possible so that all of these families that I'm talking about that are about to burst onto our homeownership stage, our homeownership markets, are able to get a loan? I agree. We're not talking about fancy new wildly creative things here. We're talking about 30 years fixed rate mortgages with housing counseling and good servicing. It's a pretty simple recipe, but we've seen that it works. As we look at the future of homeownership, I want to impress on all of you and our policymakers that it only behooves us to grow the pie. That's going to be incredibly important for our economic growth.

Let me end by picking up on one thing that you said, Doug, as we think about our immigration policy. We also need to think domestically what's going on with the immigration debate which we know is going to be a major policy conversation in 2013. If we see 11 million people in this country earn a path to citizenship, that's also going to have serious implications as housers thinking about the household formation that's going to come out of that is a major shift for our country and so we need to be thinking about that as well.

MR. DEUTSCH: My name is Tom Deutsch and I'm the Executive Director of the American Securitization Forum. We're a trade association for all the folks in the secondary market for mortgage backed and other asset backed securities both credit cards, auto loans, student loans, et cetera. I'm going to provide a little bit of context to a lot of the discussion of where were we in terms of credit availability, where was the money coming from, where was it going to.

To provide a little bit of a backdrop of where a lot of capital comes outside of the banking sector, if you think about the old view of mortgage lending that it's a wonderful life, you go down to your local bank, get a loan and you always deal with the local banker. Those days have been long gone for decades now if you think about it because at this stage most of the credit availability in the United States doesn't come through the banking sector. You may get a loan from a bank, say Bank of America, but the capital from that doesn't come out of Bank of America's pocket. Right now most of that is coming out of Fannie or Freddie or FHA, but historically that has fluctuated quite significantly whether that's coming from government markets or coming from purely private sector. This provides a little bit of a backdrop of global securitization issuance around the world, obviously the U.S. being a heavy user of credit products, Europe being a distant second and then other parts of the world. But it gives you a little bit of a backdrop of the huge amount of credit availability, a wash of credit availability from 2005 to 2007, a bit drop-off in 2008 and 2009 and then very, very slow increases.

This gives you some backdrop that the securitization markets in the United States have come back to an extent. If you look at the various asset classes, auto loans, there are not as many auto loans being made right now as there were say 5 years ago, not as many people buying cars. But generally the market is functioning, it's working. With student loans, not nearly as many student loans going to the private sector since the shift in the FELT (?) program. Most of those loans now are going directly onto the government's balance sheet. As for credit cards there are accounting changes through -- 166 and 167 that have fundamentally changed that credit card -- market. Equipment is a different -- collateralized loan obligations. This data is a little bit old. From 2011 and 2012 there are $50 billion in CLOs that were originated so that market is rapidly returning and then --

This is I think the slide that everybody talks about in various formats, the dramatic change on how mortgage credit is made in the United States over the past 6 years. This is the only slide I can possibly show you in the entire world where securitization volumes have gone up and that is the agency MBS market have gone up precipitously by $300 billion in the last 6 years. So you've got a huge change where the private MBS, effectively private credit, private investors without a government guarantee, there is a huge volume, too large of a volume in 2006 with $700 billion being put through the private label mortgage backed security system, but now that has shrunk to I think $22 billion is really overstating and a lot of that is sort of REREMIX (?) and repackaging and not really true new loan originations that are going through the securitization system. But of all the slides I have, I think this is the most telling of where is credit coming from and it's coming from the U.S. government balance sheet through Fannie, Freddie and FHA. There are lots of statistics about 90 to 95 percent of loans being made in America right now are being effectively being guaranteed by the government.

To put this in a little bit of international context, there is a lot of RMBS that's originated around the world as well. It's not just a U.S. phenomenon. Europe uses the technology quite significantly and doesn't use a government backing program. They do use a colored bond system as well that has you can argue some various backings through the banking sector, but ultimately you have a significant amount of private label RMBS originated throughout the world. But the one key thing about Europe is that much of their securities that they issue they actually retain on their own balance sheet. They keep as securities and then they keep them to the European Central Bank, so it's a way of getting credit through the government system. It's not Fannie and Freddie like, but it still has a big government backdrop here over the past couple of years. Japan, Australia, each of these will show you a little bit that RMBS is a big part of their securitization markets and where the private credit is coming from.

That gets you back to where is the U.S. now. One of the key challenges is if you want to go to a laboratory and think what's the optimal mortgage system, the problem is you can't do that. You have an outstanding mortgage stock in the United States and you have some outstanding issues, delinquencies, defaults and some of this data is a little bit dated from earlier in 2012. But it gives you some snapshots of where the delinquencies are, the significant negative equity problem in the United States where something like a quarter of the residential properties in the United States have some form of underwater nature to the mortgage so that there are still some challenges clearly outstanding in the market. The key is where do you get new credit from? Where is the credit going to come back into the system outside of the Fannie/Freddie model? There are lots of calls. You hear it from both sides of the political aisle. You hear it from Barney Frank, you hear it from Jeb Hensarling, the former chair of the House Financial Services Committee, the new income chair of the House Financial Services Committee, they both agree that Fannie, Freddie and FHA have to be drawn back somehow and in some way. How do you do that? That could be a decade long question that we're going to be continuing to answer at a political level, but this provides at least some of the basic high points of where is it that this private capital is going to come from. How does it return? One of the key questions is if you're a pension fund let's say and you've got your pension back to work, do you put that money into the U.S. housing stock market? Do you effectively through the securitization market lend that to borrowers? One of the key challenges if you're a pension fund manager is do you want to loan money to people at 3, 3-1/2, 4 percent to buy a house? Many of the pension funds' answers is no, that's just simply not enough return. The federal government may be doing that through FHA or through Fannie or Freddie, but the private markets are saying that's simply not enough return to put our money there, we're going to put it somewhere else whether that's French muni bonds or some sort of Japanese capital markets products. The liquidity of the capital markets moves pretty quickly so when you start seeing the housing market rebound, you'll start seeing the private capital come back in because there is less danger, there's less risk of home price depreciation which obviously creates some more delinquencies and defaults which then in turn creates more risk for the money that you put back into the securities market. So this is just a quick overshot of the securities market and where this capital can come back. If you think about the 2006 volume, $720 billion, that's out of the system now. How do you bring some of that back? Do we want $700 billion in private capital? No. But do we want $200 billion or $300 billion? I don't know what the number is, but it's definitely not zero. Let me turn it back to Dan.

MS. SEIDMAN: Thanks very much. I'm Ellen Seidman. I want to build on some of the things that others have said here already.

I want to add first before I really go into my major point a couple of additional points about why we ought to not settle for 10 percent less than the 2001 level mortgage market. We do run the risk of basing future policy on a very strange last 8 years and we shouldn't be doing that. Leaving aside all of the aspirational issues and issues that Janis has discussed, if we don't keep the housing market ladder robust, in other words, if we don't keep people coming in at the bottom, it becomes very, very difficult for people to move up, it becomes very, very difficult for us baby boomers to move out and that has very significant effects on the economy. To give you a couple of numbers, the boomers are going to release somewhere between 10-1/2 and 11-1/2 million homes, 80 percent of them are unoccupied single family homes, in the next 10 years. The question is who is going to buy those homes? If we don't have a system that enables the people Janis and others have been talking about to buy those homes, it's going to be a very difficult transition.

It's different in different locations. I think that one of the interesting implications of some of the conversation that we've had today is for years we've talked about the importance, and this was a critical element during the Depression with Fannie and Freddie -- Fannie was created and then subsequently Freddie, the notion of having a housing market that was the same all across the country. Now we're very much recognizing that we've got different markets and we've got different markets now, we've got different markets coming in the future. What does that mean for your housing policy? I think it's a huge question.

What I want to talk about is rental because homeownership can't stand on its own. I believe that one of the reasons we ended up with a push into homeownership, let me say before I say this, that the crazy boom of the early 2000s was heavily, heavily, heavily a refi boom and it was heavily a move up boom. It was not a first time homebuyer boom. Nevertheless, there was a huge push to first time homebuyers in part because we were doing rentals so badly and it's time to recognize that and to fix it. Over a third of the American households are renters. There were a million renting households added in 2011. This is an even greater percentage at the lower end, and we have a real mess. Vacancy rates declined from 8 percent at the end of 2009 to 4.7 percent as of the second quarter of 2012. The number of low income renters has grown over the last decade by over 2 million but we've lost 12 percent of the low rent housing units. The subsidized units, we've lost 350,000 between 2000 and 2010. We're due to potentially lose another 900,000. We need to fix this problem as well as the homeownership problem and they are two parts of the same coin in part because almost everybody rents before they own and many people rent after they own and we owe it to the entire economy as well as to the individuals to fix this.

I've got four points. We have to fix the simple availability of lower rent especially larger size units in places that are choice neighborhoods to live in with jobs. We have to stop the continuing loss of affordable rental units to conversion, obsolescence and demolition. We have to figure out, and this is going to probably take some government backing, how to have consistent financing for nonluxury and smaller buildings which frankly is where a huge percentage of the affordable stock is. Finally, I think we need to be thinking about some nonfee alternatives, the stuff between rental and ownership, so that you can have shelter and some appreciation, but you don't necessarily have to take on the full load.

MR. GAYER: Brian a few times mentioned the phase resetting, resetting policy, so as a little context on how hard this might be, we've got a long bipartisan tradition of promoting homeownership at the policy level. Google is a powerful thing. You can find speeches at least dating back to President Hoover that are virtually indistinguishable from each other on the importance of promoting homeownership. The only way you can distinguish in a blind test is before the 1990s, a home was a man's place that we needed to support and then after the 1990s it was a family's place that we needed to support apparently, and it was very obviously bipartisan. To pull a few quotes, President Clinton said, "When we boost the number of homeowners in our country we strengthen our economy and we build better citizens." And President Bush said, "Homeownership of the cornerstone of the America of vibrant communities and benefits individual families by building stability and long term financial security." I think it's fairly obvious over the past few years that some of these statements I think are overstated on the simple evidence of the importance of homeownership and in President Bush's words, "long term financial security." Homeownership peaked in the middle of the last decade which was not a harbinger of long term financial security. If you look simply across countries, some countries such as Canada have similar homeownership rates that we do but doesn't subsidize it as heavily. Other countries like Germany and Switzerland have much lower homeownership rates, where Spain for example has a much higher homeownership rate. So in simple correlations if anything it's not a key ingredient or a necessary ingredient for a strong economy contra to what the last almost 100 years of presidential speeches would suggest. I want to reiterate what Doug said that the issue here is not whether or not we should be subsidizing shelter, it's how we should apportion our subsidies between homeownership and rentership and right now it's disproportionately toward homeownership by about 4 to 1 in current policy.

People have been talking about mortgage finance and I want to focus a little bit on the tax side because that's the biggest source of subsidies for homeownership. In 2001 the mortgage interest deduction amounts to about $80 billion a year of lost tax revenue, the deductibility of property taxes is about $25 billion and exclusion of capital gains on the sale of primary residences was about $20 billion so that's a significant amount of revenue and if you look at the projections, it would be increasing depending on -- we can't go an hour without saying fiscal cliff, but depending on how the fiscal cliff negotiations to. It is a significant amount of revenue especially as Doug alluded to in a very constrained fiscal world that we face right now so that there is definitely scope and need for rethinking the distribution of our net subsidies across homeownership and renting.

The usual case, if you're going to justify that much intervention toward homeownership, by trade an economist so you would look for market failure -- and indeed there are some in the literature. In fact, Brian alluded to a few of them. There is some evidence that homeownership increases tenure, it increases civic engagement and it therefore increases investment in local public goods. I would offer three cautionary counterpoints to this. One, these estimates by the authors frequently by their own admission are highly uncertain and it's very difficult to know whether or not homeownership is leading to these positive outcomes are people who seek greater tenure and seek greater civic engagement tend to be homeowners so that empirically it's a difficult thing to even know. Secondly, even if it's empirically valid it does cut both ways and this was alluded to before. Greater tenure might make you more civically engaged in the local community. It also might make you less mobile which could also lead to labor market inefficiencies and there is some evidence to that as well. This empirical evidence suffers from the same problem as the counter studies, but it's to say that it does cut both ways. Third, I would suggest that even if we think that we should be leading into homeownership over rentership, we're not going about it the right way. We have very clunky policy as Doug alluded to also on the mortgage interest deduction in addition to subsidizing homeowner, it also is subsidizing lower down payments, more borrowing, bigger homes, more energy use so that there are better ways to do it. I don't think we're going to get rid of the system interest deduction but there are a lot of plans on the table on how to revise it I think in strategic and smart ways and to limit it. I'll conclude by saying we indeed should be subsidizing shelter across rentership and homeownership, but I think both the theory and empirical evidence suggest that we're too disproportionately focused on one rather than the other.

MS. OLICK: Thank you. We're going to do some questions now and I would urge the panel so we can get as many questions in as possible to keep the answers tight. Going back to what we talked about on subsidies and especially since we are talking about the future of homeownership, I want to get back to this point. If you take financial security as you said out of the equation in homeownership and you look at how many people are getting into a home as an investment versus as simply a place to live which historically what we were supposed to, I think you begin to talk about subsidies. I want to back to what Doug was saying. My question to you is when you talk about getting rid of subsidies for homeownership, do you believe that the Fed's purchases of mortgage backed securities which have pushed interest rates down to historic lows, A, a subsidy, and, B, a subsidy that should continue or should go away?

MR. HOLTZ-EAKIN: I think on net they are a subsidy. I don't think that's the main goal. The goal was to have a channel to expand economic activity in the United States. I would argue it's been minimally successful and the sooner they can exit their extraordinary monetary stance the better both for the Fed as an institution because it's very hard to do, and it will signal success on two other fronts. It will mean that we're growing and they're exiting and I think that's going to happen as soon as the fiscal side gets its house in order. They will get out of this as fast as Congress and the administration put the fiscal house in order. Let us take a moment to pray.

MS. OLICK: If we're moving away from homeownership subsidies, we talk about renter nation, that we've moved with this attitude away from homeownership that we saw quoted by two past presidents, and that now the attitude of the newer generations is that renting makes it more affordable, more mobile, less risk involved and if you're not again going to see the kind of home equity appreciation that we've seen which we'll never see again, then why bother? The question now is do we need to see rental subsidies? I'd like to put that back to Ellen. What kind of subsidies or what kind of help would you like to see in the rental market other than just new construction?

MS. SEIDMAN: First of all, let me say that if you take a look at the numbers, the mortgage interest deduction will cost the Treasury about $131 billion in 2012 which is more than all of the HUD outlays by 2-1/2 times of $48 billion. One point here is that we need to equalize some of the stuff we're doing already. A second point is, and I know I'm going to get pushback on this from Doug, the only part of the whole panoply of programs that is producing rental housing for lower income families these days is the low income housing -- credit. And it's producing it not just for new construction. In fact, new construction is down. It's producing it heavily in terms of rehab and renovation which is also really important because an awful lot of that stuff is in markets where if the use restrictions are allowed to expire, it will be lost for low income families.

I think another piece that got lost in all of the legitimate concern about investor/owners of small properties is that the one to four family buildings that have a lot of rental units in them were always financed as single family homes. It's very hard to get financing for that kind of housing now and an awful lot of it does need to be rehabilitated or refinanced and we need to figure out as we're rebuilding our financing system how we can effectively finance those small buildings, and it's not just the one to fours, it's up to fifties. That's not a subsidy, but it's paying attention to how the financing system affects rental and rental that's not luxury rental.

MS. OLICK: Moving into the new population of homeowners who are coming in and as Jains points out is going to be largely Hispanic, during the housing boom as we know Hispanics and blacks were targeted by mortgage lenders and in some cases terribly fraudulently targeted as we've seen in many, many lawsuits. Do you believe that the safeguards put in place by the CFPB and by federal regulators are sufficient going forward in the mortgage lending market to serve the population that's coming in?

MS. BOWDLER: I think Dodd-Frank did a great job at taking care of a lot of the retail abuses that we saw so that I think we'll see on that side a better market going forward. But the other side of that coin that we haven't quite figured out is how to make sure that good products are available. It's one thing to take the bad products out of the market, but we still need to make sure that there is enough liquidity available to make good products available, that there is enough incentive out there in the market for those good lenders to go out and affirmatively market and locate in the neighborhoods where communities of color are. We can talk all day about predatory lending, but the fact of the matter is that predatory lenders moved in to full a vacuum where good lenders weren't serving so that we took care of some of the predatory stuff, we need to make sure that our housing finance system going forward makes good products accessible.

SPEAKER: Let me say that we talked a little bit about counseling also and counseling is really, really critical, but for years in fact it has been almost entirely, and the Bank of America and other lenders do support it to some extent, but it's been almost entirely supported by a combination of the government and philanthropy. The lenders and investors benefit from it also and we need to figure out how to get a much more balanced system because the system has to be a lot bigger.

MS. OLICK: I hate to say this, but we're already getting the -- to take question from the audience so that I'm going to do that because you all went over your time. Do you want to take this gentleman right here?

MR. CHECKO: Larry Checko, Checko Communications. I was intrigued by Mr. Moynihan's presentation because he made it the responsibility of everybody else and not the financial institutions. This crisis did not have to happen. There were too many people incentivized the wrong way, financial institutions lost their moral compass and nobody had any skin in the game. I appreciate Brookings look toward the future, but if we don't go back to the past and try to rectify some of this, it's going to happen again because it seems every 10 or 15 years our financial institutions put us in this kind of a bind. I would like people to address what the financial institutions can do to rectify the future. In other words, have skin in the game. Everybody was selling these things off and it was like musical chairs.

SPEAKER: I can take a couple points to that. First there is I guess massive regulatory change in the wake of the crisis so that we talk about Dodd-Frank and within the next 30 days the Consumer Financial Protection Bureau is going to be putting out two major I would call landmark pieces of regulation "qualified mortgage" which the core of it is does the borrower have an ability to repay the mortgage? That's the simplest question that the CFPB has been grappling with for 2 years of how do you measure that, because you can put in a very simple metric like a debt to income ratio so that if you take 43 percent of your income and apply that toward your debt, that's an appropriate top end of the ability to repay and there are some rumors that that may end up somehow into the rule. The question is, the challenge for borrowers is that they all don't look alike. They all have all kinds of varying characteristics. Some may have very good debt to income ratios, they may be 25 percent, but they may have all kinds of other factors that may make them not as good of a credit, or let's say it's a retiree and may have a debt to income ratio at 100 percent, they don't make any money but they've got savings and they have good credit. Should you be able to lend to them? There is a challenge there of trying to create a rule that's a one size fits all, how do you measure an ability to repay, and you do that objectively. I think the capital markets to bring back $700 billion or $300 billion a year, whatever that number is, the people who invest that money want to know we've clearly made what is a qualified mortgage because we don't want to take the litigation risks and the like of having those loans put back to us if it turns out not to be.

SPEAKER: -- have a stake in it? Shouldn't everybody hold a portion of that loan for a while? Because the thing that got it all crazy was that people were selling these loans and nobody had a take in it. I didn't care if this young lady could pay the loan back because was selling it to someone else.

MS. OLICK: That's part of the second regulation which is QRM which is also coming out. You wanted to add?

SPEAKER: Your other question about what can banks do and referencing Mr. Moynihan's comments, he mentioned this and I wish he would have spent a little bit more time on it, that is that Bank of America has made a commitment to do principal correction on the most amount of portfolio that they can so that they can't do principal reduction on loans owned by Fannie and Freddie, that's a whole other panel that I would love to participate on in the future, but for those loans that they can, they're taking a hard look. I hope I don't get this wrong. I thought I heard him say that his average was about 150,000 which is significant. That's much more we're seeing other banks do and that commitment to do as much as they can on their own portfolio is more than other banks are doing and they deserve credit for that. We've got 11 million homeowners that are underwater and several economists have come out and said that that is a major drag on our economy for a number of reasons.

SPEAKER: May I say something?

MS. OLICK: Quickly. I want to get at least one other question.

SPEAKER: Briefly. I've had the privilege of serving on the Financial Crisis Inquiry Commission, I spent 18 months on this, and I would urge no one to adopt simplistic explanations of what went on. It wasn't just banks. There are nonbank entities involved. And it wasn't just the financial institutions. It took a lot of factors to produce the perfect storm, and I encourage you to read my dissent as opposed to the majority opinion.

SPEAKER: I have a two part question. One is the organizations that are working on behalf of your constituents, what are the conversations that you're having with the banking industry and local and state governments in creating environments with regard to affordable housing? Number two, why aren't we looking at places like Japan with regard to multifamily units that are eco energy efficient and in the long term very, very affordable?

SPEAKER: On the ecofriendly multifamily units, in fact to the extent that we're doing new multifamily construction at the lower end, there has been a movement toward much greener building and a recognition that if you can keep the operating costs down you have made an enormous dent in affordability. In terms of interest of governments in affordable housing, I think there in fact at the state and local level continues to be a huge interest. One very big problem is that the places that have been hardest hit by the housing problem have also been hardest hit in their pocketbooks and these are the places where they're having trouble paying the police and fire fighters as well as taking care of huge quantities of vacant buildings.

MS. OLICK: I think we have time for one more question.

SPEAKER: It seems that there are many forms of government stimulus for the housing bubble that we've had in the past and might have again in the future. The speaker on the end talked a lot about the government subsidies in the form of taxes, mortgage deduction and property tax deduction. The fiscal cliff gives an opportunity. I've heard some but not enough discussion of an intermediate solution by supporting homeownership keeping the deduction for your first home, not your second and not the one you're speculating to flip on and all that, that would seem a very easy solution in this time of crisis to eliminate the tax subsidies for home buying beyond the first family home.

SPEAKER: There are such proposals. The two deficit reduction commissions over the last few years proposed roughly similar reforms to the mortgage interest deduction for one, capping in a million dollars of principal interest on a million dollars of principal cap you can get 500,000 which gets more at the marginal decision of promoting homeownership than at the inter marginal decision of promoting a bigger mortgage so it's kind of eliminating the size of the mortgage, and also shifting distributionally from a deduction to credit. That again besides saving revenue, probably cuts it in half on the tax revenue side. It also shifts it on the distribution to the lower end of the income distribution. Right now the mortgage interest deduction doesn't help you if you're not an itemizer and it doesn't help you that much if you're in the lower tax brackets even and so by shifting to a refundable credit as they suggest then you shift it down and make it less oppressive so that they are out there. I think Doug alluded to this, whether or not such a thing passes is going to be extremely politically challenging. I think any attempt will be a little bit less sophisticated, it might be an across the board limit on deductions which has been proposed in various different flavors which would have similar effects but not quite the same.

MS. OLICK: I'm afraid that's all the time we have, but I'd like to thank all of the panelists and Brookings.

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