



To: Honorable President Barack Obama

Cc: FHFA Director, US Department of Justice and whosoever it may concern

Sub: **CBO Proposal to Eliminate Fannie and Freddie is Dangerous to US Economy**
[Excerpts from paper on “Coalitions of Lenders and Borrowers...,” revised in 2015,
available at <http://pro-prosperty.com/Research/Coalition%20of%20Borrowers.pdf>]

Date: January 2, 2015

Dear President Obama,

In a recent study, reported by the Wall Street Journal,¹ the US Congressional Budget Office has proposed to eliminate Fannie and Freddie (F-F) by raising mortgage lending fees sufficiently to make lending profitable for private banks. The CBO proposal is intended to let private banks take over mortgage lending business from F-F so that the F-F can be eliminated eventually.

The ‘new’ CBO proposal is yet another concoction to eliminate F-F with an utterly counter-factual presumption that mortgage borrowers are currently receiving subsidies. That subsidies are economically inefficient has been proved in a recent paper (Acharya (2011)). The fact is that the billions of dollars of profits - currently being generated by F-F and unconstitutionally (Acharya (2013)) swept away by the US Treasury through a profit sweep agreement unilaterally imposed in 2012 by the Treasury on F-F - are indeed subsidies from mortgage borrowers to (mostly privileged) taxpayers (who would have paid higher taxes otherwise) because of the higher interest rates paid by borrowers relative to the cost of capital and operation of F-F.

Whatever F-F ‘received’ from the US Treasury in 2008 – about \$187 billion - was indeed a surreptitious transfer to the ailing private banks from (mostly unprivileged) taxpayers. F-F equity was badly hit by this forced subsidy-transfer through an orchestrated government fiat called ‘conservatorship’ of F-F.

F-F have not only repaid the \$187 billion to the Treasury for the sins committed by bankrupt private banks. F-F have also been generating massive profits due to higher lending rates relative to the cost of their capital and operation. The housing sector has recovered because F-F have refinanced the mortgage loans with exorbitant mortgage interest rates being levied by private banks prior to the financial crisis.

At the current F-F lending rates and fees (which make F-F hugely profitable), private banks will only lose in mortgage lending business. Why? It is because private banks cannot recoup their lavish executive bonus, perquisite and pay or fund massive political contribution from mortgage lending

¹ “Life Without Fannie and Freddie,” Review and Outlook, Wall Street Journal, December 26, 2014.

business at the current F-F rates and fees. But the current F-F lending rates and fees have been proved to be necessary for the recovery of the housing sector as well as the economy. In other words, lavish executive bonus, perquisite and pay and massive political contributions – which are huge subsidies enjoyed by the privileged but borne by the unprivileged - are factually unsustainable, economically inefficient and catastrophic.

By suppressing the truth underlying the real economic malaise, the ‘established expertise’ in the CBO study as well WSJ commentary turns out to be factually fallacious, specious and dangerous to the US economy. The Financial Crisis Inquiry Commission has found in 2011 that that the financial catastrophe of 2008 was caused by the failure of the established experts in the academy, industry and government to see, e.g., that elimination of F-F is dangerous to the economy. It is, therefore, prudent to dissociate the failed expertise from fact-based government policy, such as: voiding the unconstitutional profit sweep agreement imposed on F-F, unilaterally by the Treasury—the government arm of the private banks—and recapitalizing and releasing F-F from conservatorship with a clear mandate to not subsidize either the privileged or the unprivileged citizens.

With profound regards,

Sankarshan Acharya

Founder, Citizens for Development & Pro-Prosperity.Com
Director, Research Center on Finance and Governance

PS: Please feel free to circulate.