Of Mortgages and Markets

The tumult in the mortgage markets is on the minds of everyone these days. It's certainly on the minds of all of us here in the Federal Reserve System.

Responding to the recent uptick in mortgage foreclosures and delinquencies is a priority for all of the Federal Reserve banks. One way we can do that is by helping policymakers, journalists, and business leaders put those trends into perspective.

The truth is that the vast majority of homeowners have been able to make their monthly home payments on time, including many that hold what are commonly known as subprime mortgages. Many foreclosures are concentrated in specific regions, and significant portions of those were the product of risky investments made for speculative purposes.

It's also important to recognize that not all foreclosures can or should be avoided. For a variety of reasons, some individuals end up with homes and mortgages that turn out to be unsustainably large relative to their current financial resources and their expected future earnings.

Yet it's hard to overstate how devastating losing a home can be to a family that was simply pursuing the dream of sustainable home ownership. Thus, the Richmond Fed has teamed up with the other banks of the Federal Reserve System to embark on the Homeownership and Mortgage Initiative.

One of our tasks in this Initiative is to lead an outreach effort that can help prevent unnecessary foreclosures. Our Community Affairs Office is collaborating with state finance housing agencies, financial institutions, and nonprofits to provide foreclosure prevention training to Fifth District housing counselors. Our outreach efforts have already contributed to the creation of a foreclosure prevention task force in South Carolina and a 24-hour counseling hotline for North Carolina residents at risk of losing their homes.

The widespread attention to home mortgage delinquencies has given rise to a push for new policy responses from state legislatures and Congress. The risk with such responses, however, is that the policy outcomes may be too hasty and based on uninformed perceptions instead of hard facts.

So, another element of the Richmond Fed's contribution to this effort is our research capability. In an effort to provide financial institutions and policymakers the detailed analysis that can help craft evidence-based policy solutions, we have taken the lead on coordinating a working group consisting of some of the System's top economists and community development experts. Their task is to prepare an overview of the current state of knowledge about housing and mortgage markets. The System will then conduct further research to fill the analytical gaps and better understand the effects of foreclosures on neighborhoods.

The Richmond Fed is also distributing mortgage data and providing analysis to help Fifth District communities identify where foreclosure "hotspots" exist and convening discussions with policymakers and practitioners to understand the underlying causes of foreclosures. In the first quarter of 2008, we have made presentations in the District of Columbia, Virginia, and North Carolina.

We are also taking part in a process that will review and propose updates to the Truth in Lending Act and related statutes. Our hope is to restore some of the underwriting safeguards and disclosure standards that have been eroded in recent years.

There is no question that the U.S. economy is going through a period of adjustment which is quite uncomfortable for some. Yet it's important to remember that a competitive market economy is, over the long run, better for everyone. The cover story on private equity funds in this issue of *Region Focus* is a good reminder of that. For all the bad press they've received over the past year, private equity funds serve a very important function: They help make the allocation of capital in the economy more efficient.

By purchasing companies that are underperforming, private equity funds are able to enhance a firm's productivity through restructuring. And despite the coverage of the short-term layoffs that often occur after a private equity takeover, what isn't often reported is the large number of new jobs that are eventually created by the newly efficient firm. In short, private equity helps facilitate the vibrant competition that is the key to innovation and healthy economic growth.

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