



GSE Activity Report

Thursday, June 22, 2023

Buying Freddie?

Summary

A [Bloomberg article](#) tells a fascinating tale of high-flying personal real-estate investment and other alleged acts of self-dealing at the expense of the seemingly-hapless Federal Reserve Bank of San Francisco. Internal controls may come and go, but the striking policy take-away from the reporting is that Bank employees launched a credible Home Loan bank System effort to acquire Freddie Mac. What next?

Impact

An FHLB acquisition of Freddie would have taken the GSE back to its pre-1989 roots as the S&L's window into the secondary market, not that there are all that many thrifts left to revel in newfound private access to an "effective guarantee" even better than the FHLBs' own implicit one. The mechanics of an acquisition of Freddie would have had to deploy the System's capital – minimal to be sure but still sufficient to float a deal at a time of low advance demand – to get a new earnings source for a System long hoping Congress would expressly authorize it to securitize mortgages.

The reasoning would also have to be that members would have strongly approved this because once Freddie was owned by the System, those who owned the System owned a GSE that could serve their wishes far better than Fannie and Freddie on their own generally are willing to do. Insurance-company members of the System might have salivated particularly quickly at the prospect of their own window into the CMBS market.

Given the GSEs' low capitalization at the time (somewhere around 2018), the deal could even have been cheap even as it made the GSEs' litigious private shareholders – close associates of the FHLB-SF employees – a pretty penny without the need to continually hound one appellate proceeding after another.

What scotched the deal, which the news report suggests wasn't just doomed by lack of trying? For one thing, it would have required all the Banks to agree, often a Herculean undertaking. It would also have required FHFA approval under statutory authority which we think at best vague as to whether the System can do more than issue cost. Could the Office of Finance have owned Freddie if enough FHLBs wanted it to? We'll never know – or at least one thing we'll never know – but this seems at least a challenging transaction structure.

Outlook

What's even more interesting than the complex tale of personal profit and Systemic ambition is the reminder that even in conservatorship Fannie and especially its smaller and more affordable rival, Freddie, are hybrid entities owned by private shareholders as well as, via direct and indirect obligations, the U.S. Government. With recapitalization, the GSEs are more expensive than they were but totemic deals over recent years make it clear that price is usually no object. The key to the GSEs' future is what Treasury wants to do with them and 2024 could be another turning point for those with ambitions to profit off charters Congress remains reluctant to redesign.