Home Loan banks could be doing much more to support affordable housing

By Rev. Luis Cortés Jr. May 22, 2023, 10:00 a.m. EDT 5 Min Read

I have the honor of serving as the founder and CEO of Esperanza, a nonprofit community development corporation confronting poverty, disinvestment, blight and the lack of economic opportunity in the low-income Hunting Park neighborhood of Philadelphia. I understand the growing challenges facing Hunting Park and urban and rural low-income communities across America. During my 20-year service as an independent board member of the Federal Home Loan Bank of Pittsburgh, which ended in 2021, I learned the Federal Home Loan Bank System can do much more as a government sponsored enterprise to support affordable housing.

As the Federal Housing Finance Agency is in the report-writing phase of its monthslong comprehensive review, "The FHLBank System at 100: Focusing on the Future," it is the perfect time to consider new Home Loan bank affordable housing efforts. During the COVID-19 pandemic and the March 2023 banking crisis, the Home Loan banks satisfied member liquidity needs. However, during the ongoing housing crisis, their affordable housing work has been business as usual. While Home Loan banks are meeting member liquidity needs in all market conditions, they are not leveraging the strengths and unique features of the system to support affordable housing.

The Finance Agency is first and foremost the system's prudential regulator, but it is also the steward of the public interest. The agency's forthcoming report should chart a new course for both the regulator and the system to establish a more equitable distribution of the system's government-supported earnings between the member/owners and the broader public. The report should lay out a systemwide approach that incorporates affordable housing into the planning, development and execution of Home Loan bank activities while not weakening the system's safety and soundness or its role as a reliable and low-cost source of member liquidity.

The Home Loan banks' future should be guided by a mission defined by regulation, supported by existing statute and built around the central functions of providing member liquidity and supporting affordable housing. The mission should ensure the current support of member liquidity does not waver, but that the Home Loan banks also create new mechanisms to support liquidity for long-term funding of affordable housing, including rental housing. This work should occur outside the framework of the affordable housing program and include focus on long-term funding supported by member institutions and capital markets. This mission must be supported by the full range of Finance Agency supervisory and regulatory actions, including examinations, board guidance and the structure of Home Loan bank executive incentive compensation.

As one of several efforts needed to increase Home Loan bank support of affordable housing, the Finance Agency should lead the system to update a 2011 emergency action to build capital. This would double Home Loan bank affordable housing financial support without legislation, not weaken Home Loan bank capital and allow payment of member dividends.

Coming out of the Great Recession, the Home Loan banks' weakened financial condition threatened their capacity to provide member liquidity. In 2009, Moody's projected that eight of the 12 banks would fall below regulatory capital requirements. The Finance Agency's 2010 report to Congress said, "The condition and performance of six of the 12 FHLBanks are less than adequate."

In 2011, the system had few options to build capital quickly, but had satisfied the 1989 obligation to provide 20% of net income to support taxpayer funding of savings and loan cleanup bonds (Resolution Funding Corporation or REFCORP). With the support of the Finance Agency, the Home Loan banks moved to capture that 20% of income to fund a new subset of retained earnings known as restricted retained earnings. This action was taken without new legislation or regulation and there was no opportunity for public comment.

With the rest of the board of directors of the Federal Home Loan Bank of Pittsburgh, I supported this 2011 emergency action to ensure Home Loan banks could meet their members' liquidity needs. I now support revising the restricted retained earnings rules to allow more effective Home Loan bank affordable housing efforts in this crisis.

In 2023, Home Loan bank capital is well above regulatory requirements and profits are strong, but their affordable housing efforts are less than adequate. The system closed 2022 with a 133% increase in loans to members over year-end 2021. While no public data is currently available, it is likely advances are now above year-end levels. Restricted retained earnings have risen to over $6 billion. Higher interest rates are good for Home Loan bank earnings but bad for the development of affordable housing.

The Finance Agency should direct the Home Loan banks to devote the investment income from restricted retained earnings to support affordable housing while not touching the restricted retained earnings themselves. Based on 2022 year-end financial information published by the system's Office of Finance, the 2022 investment income from restricted retained earnings was approximately $350 million. This is almost exactly equal to the statutory 2022 affordable housing program assessment of $355 million. These funds should not be added to the affordable housing program but should support new Home Loan bank efforts to build liquidity for long-term funding of affordable housing that leverages Home Loan bank and bank member support.

The Finance Agency's review of Federal Home Loan banks should result in proposals that leverage the unique strengths and structure of the system to better support affordable housing. To bring meaningful change, all of these initiatives will require a supportive regulator and Home Loan banks that contribute expertise and thought leadership. The Home Loan banks and their boards of directors should use this moment as an opportunity to reposition the system for the future, not to fight for a status quo that does not serve the broader public. The success of these efforts will improve liquidity for the financing of affordable housing in communities across America and will make the Home Loan banks more relevant and important than ever before.

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