Speeches

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OTS-083 - Remarks by Ellen Seidman, Director, Office of Thrift Supervision, To Eighth Annual Economic Development Summit Greenlining Institute, Sacramento, California, March 14, 2001

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It is a pleasure and an honor to be with you here this evening. Today's huge turnout and the quality of the presentations and the discussions is a testament to the effectiveness of Greenlining's work.

The question of how to meld housing affordability with neighborhood stability and quality of life is one of at least a century's standing in the United States

At the turn of the last century, the "discovery" of tenement housing and urban slums sparked major improvements in public health and public education. These same concerns also gave rise to modern zoning and the beginnings of suburbanization.

At the end of the Second World War, massive demographic shifts, including in particular the migration of African Americans to northern cities and the huge bulge in home-coming veterans, who had previously not headed households but were ready to start families quickly, brought the issue to center stage again, as both groups demanded affordable housing, and the country responded in a largely segregated fashion.

The fifties brought urban renewal and highway construction, often destroying stable and affordable urban communities and those displaced were thrust back into the search for affordable housing in a good place to live.

In the seventies and eighties, we bemoaned the death of rivers, air quality and cities, and did something about the first two while leaving the cities largely to fend for themselves, as those who could searched for their affordable nirvana further and further out in the hills and cornfields. These were also the years in which significant Latino and Asian immigration began a slow but steady trend toward revitalization of some of the cities, particularly in California. But few noticed.

By the nineties, we began to focus on what we had wrought: sprawling metropolitan areas with dying cities at the center and, for those "lucky" enough to get out, longer and longer commutes to work from less and less functional and financially unstable exurbs, fragmenting families and often encroaching on prime farmland. Over the last two decades, the population of greater Los Angeles grew by slightly less than half, while the geographic area it covered tripled.

Of course, one of the great stories of the nineties has been the revitalization of many of America's cities, including some of the previously worst hit. Populations are up, jobs are up, real estate prices are up, crime is down, and today's *Wall Street Journal* reports there is an apartment boom in downtown Los Angeles. It's a wonderful story, and many of those in this room deserve much of the credit. But along with the revitalization has come pressures on affordability--the urban places that were once shunned are becoming out of reach to even middle income families, pushing them, too, into the exurban search.

Americans on both coasts and in some other parts of the country face similar problems. But in California, those who need affordable housing, many of them minorities, have been hit especially hard.

In May 2000, the California Department of Housing and Community Development reported:

a) If current trends continue, California will build less than 60 percent of the new housing units needed to accommodate projected 1997-2020 population and household growth.

b) As of 1995, more than half of California's 2.5 million low-income renters paid more than 50 percent of their incomes for rent; by 2020, total unmet affordable housing needs in California will rise to about 3.7 million units.

c) As of late 1999, while the U.S. homeownership rate hit a record 66.8 percent, California lagged at 55.7 percent -- and those

Californians lucky enough to be new homebuyers had to travel twice as long to work each day as new homeowners in other parts of the country.

d) California cities are finding it ever more difficult to fund housing-related public facilities and infrastructure; in some jurisdictions, impact fees and required exactions already exceed $30,000 per unit and account for more than 15 percent of total housing production costs.

The report concluded, "it is housing that is at the root of many of today's hot policy issues."

So what's the solution? The DHCD report suggested both a "stronger and more-broad based commitment to producing more housing, more diverse housing, and less expensive housing," and cited in particular, the needs to:

- Expand the supply of mortgage credit available for new multi-family housing;
- Increase infill housing, especially multifamily infill housing;
- Inventory true environmentally sensitive and "heritage" lands so other land becomes available for housing; and
- Improve the land planning and entitlement process, including encouragement of well-designed new towns and streamlining the regulatory process.

In other words, California needs to grow smart in an environmentally balanced way.

These are difficult challenges for any community, and for California, with its strong environmental and local option traditions, it may be

especially hard. But the projections make clear that the very life style that Californians value is at risk unless some action is taken.

What can we as bank regulators do? First, let me say I think it's extremely healthy that the question of affordable housing for people of modest and middle income is finally being framed as a multi-faceted issue involving concerns as diverse as wetlands preservation and job locations as well as financing. For too long, there has been an assumption that if you can just put the financing package together, the affordability problem will be licked. When land prices and impact fees outpace incomes, that just isn't so. On the other hand, how housing gets financed--from pre-acquisition planning funds through acquisition, development and construction to permanent financing--is still a critically important part of the picture.

One of the most important contributions we as regulators can make is to have--and to make certain our examiners have--a realistic view of the actual risks of these transactions and to understand how those risks can be successfully managed.

Last month, OTS piloted a course for relatively experienced safety and soundness and compliance examiners on housing and community development. The object of this week-long course, which follows on an affordable housing course we initiated a few years ago, is to make certain that examiners understand the full dynamics of how this business works today, who all the partners are and what their roles--including their roles as risk-mitigators--are, how to evaluate them, and how to evaluate the manner in which the institutions are managing risk, including reserving and capitalizing against it.

We want examiners to avoid either of the two classic mistakes: either assuming that a "good guy" loan <u>must</u> be a risky loan, even though the risk may be much smaller than that of other loans in the portfolio, or not understanding the loan and thus not effectively

evaluating whether the institution is in fact managing the risk that does exist properly.

We're also doing research on the actual loss performance of various types of loans in comparison to each other. While this research is only preliminary, and is hampered by lack of some kinds of data, initial results confirm what most people in this room know--that real estate lending is, over very long periods of time, very substantially less risky than commercial lending, and by a factor greater than that recognized in the risk based capital rules. The first paper from this work went up on our web site today in connection with a proposed regulation that will reduce OTS capital requirements for certain home, land and construction loans.

For OTS and the thrift industry, of course, real estate lending has special meaning, both positive and negative. Having listened to and participated in monthly discussions among our senior supervisory staff for more than three years now, I can tell you that they remember all the warning signs of lending on wishful thinking. However, they also are very supportive of the industry's real estate lending, including ADC lending, when it is well underwritten and well managed. So those of you who still have thrifts in your midst, talk to them; housing is their bread and butter.

Finally, as many of you know, the OCC has been working on a revision of its loans-to-one-borrower regulations to, among other things, enable small institutions to better serve those who are engaged in some types of housing development lending. We've been following the OCC's process with great interest, as our statutory authority is tied to theirs. As quickly as possible after OCC adopts its new regulations, we will revise ours.

The vast majority of institutions OTS regulates are community banks in the purest sense of those words--they are geographically oriented and their long-term health is tied to the health of the communities they serve. We therefore believe strongly that as a matter of safety and soundness, going well beyond Community Reinvestment Act obligations, thrifts need to be involved in their communities and to help them prosper. And given their heritage and expertise, helping communities make certain they have an adequate supply of housing, at all income levels, so those who make communities livable places can live in them, is something thrifts are particularly good at.

California is in a serious bind on the issue we started out with--how to house its citizens in a manner that is both affordable and livable. Greenlining, its members and the financial institutions that have worked with it over the years are in danger of losing what has been gained unless the challenges outlined are taken up and resolved. As we're now recognizing, the challenges, and thus the solutions, go beyond financing. But for the large part financing plays, thrifts, with the strong support of their regulator, are ready to help.

Thank you.