A Reality Check on GSE Privatization

June 4, 2025

Recently, there has been a renewed push from policymakers in Washington to explore the privatization of the government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. Given the importance of implied or direct government backing of the mortgage market and its benefits to the private sector, there appears to little net benefit to fully privatizing the GSEs.

Fannie Mae and Freddie Mac play a central role in the US housing finance system. These GSEs were created to stabilize the mortgage market and promote homeownership and access to credit, particularly for low- and moderate-income households. The 2008 financial crisis marked a turning point when the GSEs were placed into federal conservatorship; however, in the years since, they have returned to profitability and repaid the Treasury in excess of the original bailout amount. Their continued operation under conservatorship has allowed for tighter oversight and risk-based pricing, which has helped protect taxpayers from future losses.

Households have also benefitted from these GSEs. By providing liquidity and standardization in the secondary mortgage market, GSEs have helped keep mortgage rates lower than they might otherwise be — especially during periods of market stress, such as the Covid-19 pandemic. Their support for 30-year fixed-rate mortgages, in particular, has offered long-term affordability and stability for homeowners. Innovations in credit risk transfer and capital frameworks have further reduced systemic risk while maintaining broad access to mortgage financing.

Privatizing Fannie Mae and Freddie Mac would represent a fundamental shift in the US housing finance system. We see the major implications as follows:

- **Higher Mortgage Rates:** Privatized GSEs would lead to tighter credit standards and higher mortgage rates, as investors in agency mortgage-backed securities (MBS) demand higher yields to compensate for the reintroduction of mortgage credit risk. Current market data supports this concern; non-agency mortgage rates generally charge higher yields than loans underwritten to GSE lending standards. This could reduce access to affordable home financing, especially for first-time buyers and underserved communities.
- **Increase Home Price Volatility:** The housing market could experience increased volatility in the absence of a government-backed stabilizing force. During economic downturns, the GSEs have historically played a countercyclical role by continuing to provide liquidity when private capital retreats. Privatization could weaken this function unless alternative mechanisms — such as a government mortgage insurance fund or a public utility model — are put in place.
- **Protracted Timeline:** The timeline to disentangle the GSEs from the Treasury would be lengthy and potentially problematic. The process depends on the political will and regulatory changes involved. Privatization will require coordination between the Federal Housing Finance Agency (FHFA), the Treasury, and potentially Congress for legislative approval. Coordinated action across multiple layers of the federal government would likely span multiple presidential terms.
- **Recapitalization:** While privatization would result in funds potentially flowing to the US Treasury via the equity sale of the GSEs, a significant amount would be required to recapitalize the now-private entities. The GSEs have been allowed to retain earnings since 2019 to begin rebuilding capital buffers. However, under current capital requirements set by the FHFA, both Fannie and Freddie would need to accumulate roughly $250 billion dollars in capital to meet the thresholds required for safe operation outside of conservatorship. This process alone could take 5 to 7 years through organic earnings growth.

- **Government Backstop Could Remain:** Privatization could, in theory, transfer risk from taxpayers to private shareholders and creditors. However, without a clear and credible resolution framework, taxpayers may still assume some level of government support in a crisis, potentially limiting the fiscal benefits. Moreover, if privatized entities were to face financial distress, the government might still feel compelled to intervene, similar to 2008.

The push to privatize Fannie Mae and Freddie Mac may generate headlines, but in reality, the implications are clear: the risks tied to full privatization outweigh the potential rewards. The GSEs have played a key role in keeping mortgage markets liquid and stable, especially during downturns. Their current conservatorship model has allowed for tighter oversight and steady returns without exposing taxpayers to undue risk. Privatization could lead to higher mortgage rates, tighter credit, and more market volatility. The long and uncertain path to privatization combined with the likelihood of continued government involvement in a crisis also add to the complexities around privatization.

For now, the more compelling investment thesis lies in monitoring how the GSEs evolve within the current framework, rather than positioning for a full exit from government control. We maintain a constructive view on agency MBS, given the continued support from the GSEs and the structural benefits they provide to the housing finance system.