Possible backfire in Paulson’s rescue plan

United States Treasury Secretary Henry Paulson announced his rescue plan for mortgage industry giants Fannie Mae and Freddie Mac back in mid-July claiming that the outrageous impending costs would never materialize. Paulson hoped the presence of government backing would restore consumer confidence and in turn make it easier for both companies to raise desperately needed capital and therefore be able to maintain favorable rates necessary for borrowing.

Only weeks have passed since the announcement of the rescue plan and its intentions, but the market has proved Paulson otherwise. Throughout the past week both Fannie Mae and Freddie Mac’s lingering market capitalization has virtually eliminated. The two companies are now in a position where they have to pay higher interest rates on their bonds.

Fannie Mae decided to dip into the subprime loans and “Alt-A” mortgage markets in 2006 and 2007 and now owns or guarantees $388.3 billion worth. With home values continuing to fall, according to washingtonpost.com, Fannie and Freddie have “little or no prospect of raising enough private capital to bolster their perilously thin resources.”

The Post goes on to say that if the two companies “can't borrow extra-cheaply and pass those savings on to home buyers, the very reason for their special status as ‘government-sponsored enterprises’ is in doubt.”

In order for Mr. Paulson’s rescue plan to do what it was intended to, it needs to be put into effect sooner rather than later. A few things need to happen to get the ball rolling. First, it is necessary for the government to pledge its support for Fannie Mae and Freddie Mac including the bonds they own and the mortgage debt they guarantee. Second, the two mortgage giants need to be given an adequate amount of capital to stay a float until the housing market hits rock bottom.

Once in motion, a currently tumultuous market could become one of serenity.