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The Mortgage Industry Has Some Questions and Concerns About The Road Ahead

Any discussion about the challenges faced by a particular industry or even by a particular household requires the same acknowledgement right up front: the most devastating pandemic in modern history has unfortunate consequences for just about everyone. It's also important to remember how much those consequences can vary and to consider how that everything is relative when it comes raising concerns at this particular moment in human history.

Truth be told, if I only had a few clients with a few superficial gripes about their stark new realities, I wouldn't have anything to write about here. But the fact is that the mortgage market is facing a massive existential threat that will manifest itself in ways that may not be readily apparent to policymakers. These are the questions and concerns that need to be on the table for discussion.

1. **Careless CARES Act**

Granted, I'm not a politician and won't pretend to know all of the considerations that could have led to the final wording of the relief bill, but we at least need to ask why it included such an open-ended invitation for homeowners to skip mortgage payments for up to 360 days without demonstrating a financial need to do so. Why does the legislation prevent mortgage servicers from taking steps to prevent abuse? As it stands, people that are still very much employed and with plenty of cash to continue making payments are requesting forbearances simply because no one can stop them. The CARES Act specifically forbids it!

2. **Forbearance has unintended consequences for homeowners.**

If you have a legit financial need to skip payments, power to you! This legislation was made for you and everyone is hoping your financial situation allows for business as usual on the other side of this COVID drama. But please be aware that things won't get back to normal right away, EVEN AFTER you're able to start making payments again. While it's true that the CARES Act prohibits negative credit bureau reporting during a forbearance, that doesn't mean it won't happen accidentally given the gigantic strain being placed on mortgage servicers right now. Yes, you will be able to fix any legitimate inaccuracies eventually, but they could still prevent you from moving on with your life when it comes to obtaining credit in the intermediate future.

MBS & Treasury Market Data

	Price / Yield	Change
MBS UMBS 6.0	99.06	-0.37
MBS GNMA 6.0	100.08	-0.17
10 YR Treasury	4.7023	-0.0016
30 YR Treasury	4.8114	-0.0025

Pricing as of: 4/25 9:59PM EST

Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.52%	+0.13	0.00
15 Yr. Fixed	6.91%	+0.08	0.00
30 Yr. FHA	7.00%	+0.13	0.00
30 Yr. Jumbo	7.68%	+0.10	0.00
5/1 ARM	7.55%	+0.15	0.00
Freddie Mac			
30 Yr. Fixed	7.17%	-0.27	0.00
15 Yr. Fixed	6.44%	-0.32	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	7.24%	+0.11	0.66
15 Yr. Fixed	6.75%	+0.11	0.64
30 Yr. FHA	7.01%	+0.11	0.94
30 Yr. Jumbo	7.45%	+0.05	0.56
5/1 ARM	6.64%	+0.12	0.87

Rates as of: 4/25

Moreover, you really need to be aware of how the mortgage market will treat those in forbearance when it comes time to get your next home loan. Even though there will not technically be derogatory information on your credit report (assuming no mistakes are made, or that they've been cleared up), **you may not qualify** for another conventional loan for months **AFTER** your forbearance has been brought current, and you definitely won't qualify if you are still paying back a forbearance deficiency.

This raises another critical point: how do you bring it current? What happens after you're done skipping payments? The answers to this vary based on your mortgage servicer, but one of the most common initial answers is that you're on the hook for the lump sum of payments you missed. The official answer from the FHFA is as follows: "At the end of the forbearance period, the homeowner will work with their servicer to **repay all past due amounts and accrued interest**. Homeowners unable to resolve past due amounts, or who need a lower mortgage payment, are evaluated for longer-term borrower assistance options such as a loan modification."

Those who have had to deal with loan modifications in the past know that it doesn't often work out as simply as it might sound. And there too, your ability to qualify for the best mortgage programs may be limited in the future.

3. **Unintended consequences for the mortgage industry**

This has been the subject of much debate, speculation, and advocacy inside the industry. But here are a few key pain points that may end up being more than merely painful for some lenders.

- A loan in forbearance cannot be delivered to Fannie/Freddie and many of the biggest buyers of mortgages are similarly unwilling to take these loans. That means the small-to-medium mortgage lenders who fund loans with their own money or with their own credit lines will be stuck holding these loans. They'll have no way to move them off their books or off their credit lines and will effectively be closed for business due to a lack of liquidity.
- It gets worse. Those same lenders are already retroactively on the hook for any loans they just sold to larger entities in the event those homeowners decide they need forbearance before making their first few payments. The lightest penalties would be equal to or greater than whatever premium the buyer paid for the loan. And in many cases, due to a steep decline in servicing valuations (also caused by the CARES Act) that premium merely meant the originating lender was breaking even. In the most extreme cases (though not uncommon), originating lenders were effectively paying loan buyers to take inventory off their hands. And even in those cases, the lenders will still be penalized if the loan goes into forbearance before the first few payments are made.
- Mortgage servicers are on the hook to provide timely interest payments to mortgage investors regardless of the payment status of the underlying loans. In some cases, it's principal and interest. The FHFA director says this isn't his concern and that other servicers have the cash to step up and service those loans. Translation: the biggest banks will be able to vastly expand their servicing portfolios for pennies on the dollar (they won't pay full price to bail out smaller servicers). This threatens to cripple industry and leave only the biggest banks intact, because the servicers at risk account for a huge portion of both the servicing AND origination pieces of the mortgage market.

Again, FHFA doesn't see all these downsides in the same way, but others disagree. My contention is that FHFA is severely underestimating the propensity for people who don't NEED a forbearance to request one anyway. And remember, it's not a request. Mortgage companies can't verify the hardship and can't deny you. But also remember (in case you're reading that and thinking it sounds like a great deal for you), there is that laundry list of unintended consequences that no one is telling you about (see #2 above).

That's beside the point when it comes to the servicing drama, however. Whether or not anyone feels the FHFA SHOULD care, they're not in a position to solve the big issue for servicers. That help will have to come from Treasury or from the Fed with Treasury's blessing. Here's an important story on those efforts.

What FHFA CAN do is to offer clarity and guidance about how we will get back to a functional mortgage market in the future with a massive contingent of prospective borrowers who have been flagged as having a forbearance on a previous loan. Borrowers need to know before they can make informed decisions. While we're at it how about some relief for the honest, hard-working small-to-medium lenders out there who are going to get hit hard if their recent pipeline of clients opts for forbearance? Should they be retroactively punished?

This would be like an employee being laid-off due to the coronavirus pandemic and then being forced to pay back previously earned income. The mortgage investors buying these loans in forbearance certainly have a right to be made whole, but their beef should be with the wording of the CARES Act and not with the mortgage lenders who have been and would like to continue to be valued business partners for years to come.

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