News From the FAMP Government Affairs Committee

MBA Cuts Loan Forecast Again, Cites Lagging Home Purchases

by Brad Finkelstein
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The Mortgage Bankers Association has cut its 2014 loan origination forecast to $1.05 trillion because home purchase loan application volume is well behind where it was this time last year.

There is weak demand for housing because of slow growth in employment and wages, said Michael Fratantoni, the MBA's chief economist, said Monday at the group's National Secondary Market Conference in New York. In January, MBA predicted volume would total $1.12 trillion in 2014. Last year, the industry produced about $1.8 trillion in loans.

Despite the gloomy forecast, Fratantoni says purchases should start to rebound in the second half of this year and continue to grow in 2015 and beyond. This year "is the floor we are going to build on," he declared.

It's a hard floor, though.

Even if rates continue to drop as they have in recent weeks, Fratantoni does not expect an increase in refinance activity. He predicts refinancings to remain in the area of $100 billion per quarter for the next couple of years and even likely beyond that. Not only will there be fewer refinancings seeking reductions and rate and terms, in the next few quarters there will be fewer loans being done through the Home Affordable Refinance Program.

The missing piece of the equation to see the increase in the purchase market is home affordability. The lack of homes for sale is good for prices, but not for the mortgage market.

Home prices should continue to increase in the short term, but the pace is apt to slow as builders start to meet demand and more property owners who are no longer underwater decide to sell their homes.

As for how the overall economy affects the purchase market, if unemployment were to decline another one-half of a percentage point, that would cause wages to increase, making buying a home more affordable, Fratantoni said.

Unemployment is also affecting household formation, which means there are fewer people looking for a home, whether it is to be purchased or rented.

Interest rates for the 30-year fixed rate mortgage should be at 5% by year-end and 5.5% by the end of 2015. Fratantoni expects the Federal Reserve to continue its taper program and reduce its mortgage-backed securities purchases. In addition, the Fed should start raising short-term rates in the second quarter of 2015.

A wild card is the international environment, such as the current situation in the Ukraine. Historically, there has been "a flight to quality" by investors during these times, looking at the financial safety that Treasuries offer. When the demand for Treasuries increases, their interest rate decreases - and mortgage rates typically follow suit.

This time around, Fratantoni expects the situation to be resolved quickly and rates to start to rise again.

Another reason why purchase activity is lower, especially in the conforming loan area, can be attributed to many lenders starting last fall to prepare for the qualified mortgage rule and ability-to-repay requirements by cutting their loan product offerings.

On top of which, Fannie Mae and Freddie Mac raised their guarantee fees as part of the government's plan to attract more private capital.

Meanwhile, Federal Housing Administration volume was hurt by an increase in the mortgage insurance premium and a requirement for the loan to remain insured throughout its life.

Student loan debt burdens are also affecting the ability for lenders to make mortgages where the borrower's total debt-to-income ratio is lower than 43%, Fratantoni says.

QM is also the reason why the adjustable rate mortgage market has failed to gain much share as rates have increased in recent months. ARMs usually become more popular in a rising rate environment because the starting rates are lower than fixed rates on offer.

But QM requires that borrowers be underwritten to see if they can repay through the first five years of the loan. With that rule in place, doing shorter term ARMs, such as those where the rate is fixed for the first three years before adjusting annually, does not make a lot of sense anymore, Fratantoni says.