The Down Payment Report

News and Data on Residential Down Payments

July/August 2021

Report Released: August 26, 2021

Ginnie Mae's risk-based capital rule would punish first-time buyers

Ginnie Mae's revised capital rule unleashed a flood of criticism, not just from the lenders directly affected but from respected industry leaders. The Urban Institute's Laurie Goodman, Karan Kaul, and Ted Tozer said:

"While well-intentioned, the risk-based capital requirement, as proposed, is highly punitive for nonbanks. It will likely disrupt mortgage servicing values and raise mortgage rates for Federal Housing Administration (FHA) and US Department of Veterans Affairs (VA) borrowers, who will pay for any adverse impact on servicing values."

Most borrowers who use government-insured low-down payment loans are first-time buyers who cannot afford to put 20 percent down in these times of double-digit price growth driven by shortages of affordable homes. As Congress and the Biden Administration consider ways to make homeownership more accessible to first-time buyers, it makes no sense to increase borrowing costs for government-backed loan programs.

Stay safe and be well,

Rob Chrane
CEO, Down Payment Resource
rchrane@downpaymentresource.com

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THE DPR INTERVIEW

A regular feature of the Down Payment Report, the DPR Interview showcases national leaders in homeownership assistance and low down payment programs.

Educating sellers and agents about FHA loans in hot markets

Lisa DeBrock
Division Director, Homeownership
Washington State Housing Finance Commission

Over the past six months, Washington State has been home to some of the nation's hottest markets. In May, Spokane's real estate market had the highest rate of bidding wars among the top 50 metro areas nationwide. In January, Tacoma was the hottest market in the nation, with half of all homes pending sale in just 23 days. In January, more than 4,500 homes in the Seattle market sold for $100,000 over the asking price through June.

Many families using down payment assistance from the Washington State Housing Finance Commission (WSHFC) compete with buyers using conventional financing. Lisa DeBrock, WSHFC's homeownership director, leads efforts to correct myths and educate sellers and their agents about the commission's FHA-based Down Payment Assistance program.

Q: Are fewer buyers using down payment assistance because of competitive markets and bidding wars?

Most of our families are low to moderate-income families who definitely need down payment assistance. Unfortunately, it can make their offers less competitive because sellers and real estate agents often don't know that DPA offers can be far more substantial than a regular FHA or conventional offer (not counting all-cash offers, of course). A lot of education is needed.

Q: What are you hearing from lenders about FHA loans in this competitive environment?

In my experience, sellers' perceptions are based on what they hear about FHA from their real estate agents. For example, many agents think that FHA appraisals are more difficult than conventional ones. Any appraisal of an older home might raise concerns that need to be addressed for the home to qualify, but loan officers tell me that the cost to bring these properties up to par is usually minimal.

We need to educate sellers and their real estate agents that the cost of repairs to qualify for an FHA loan is usually small. For whatever reason, the industry has a perception that a conventional offer is a stronger offer, whether that is true or not. If you have a qualified buyer, you have a qualified buyer. Whether the loan is VA, FHA, conventional, the appraisal of the property itself should not differ much from one to the other.

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(*DPR Interview* continued)

Q: Is this problem getting worse in your market because it is getting more competitive?

Yes, pretty much every affordable home I hear of has multiple offers on it. It doesn't matter where in the state. The prices have gone up tremendously. It is a very, very tough ride for first-time homebuyers. Still, some of them are getting offers accepted because we still have strong reservations.

Q: Have you heard of a specific case where a seller took a conventional offer over an FHA offer even though the FHA offer was higher?

I'm sure that has happened a lot. When our borrowers get their offer accepted even though there were multiple offers, it's usually because of a huge education process and the reputation of the buyers' agent and the loan officer for getting these offers accepted and closed within the time frame. They can demonstrate that they have had many of these transactions this year and got them done with no time to waste. With DPA, it is a stronger deal because there is no sourcing of the funds. Our funds are guaranteed.

Q: How has your FHA business fared over the past couple of years?

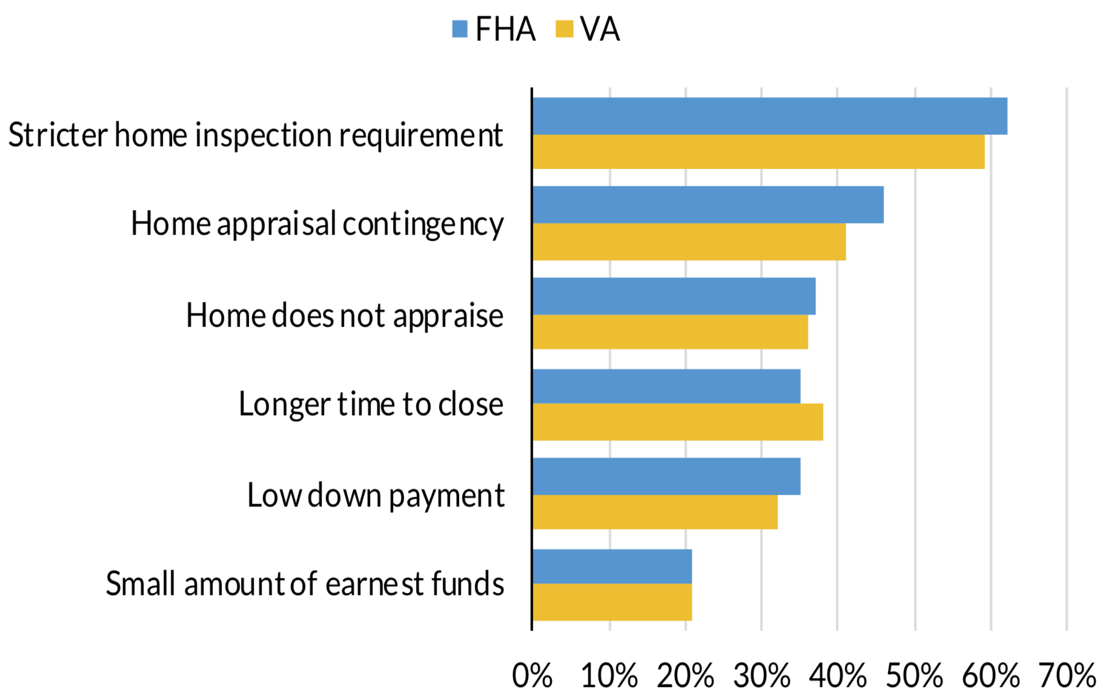
The decline in conventional financing started two years ago when the HFA preferred product was severely rolled back by Fannie and Freddie. Before that, in our whole portfolio, reservations were usually about 40 percent conventional and 60 percent government. Since Fannie and Freddie made those changes, we are roughly 18 percent conventional, which is very unbalanced. Even our current trend in reservations is roughly 20 percent conventional and 80 percent government. I really thought that we would see conventional offers increase because conventional are perceived as stronger, but we haven't. In my opinion, it's because, with Fannie and Freddie, it is very, very hard to get a borrower with a below-680 credit score approved. So, until Fannie and Freddie relax their guidelines, I think we will still see a majority of our families go FHA.

Government-insured loans

The FHA and VA Market Shares are Shrinking

A recent survey of its membership by the National Association of Realtors found that 89 percent of sellers would be likely to accept an offer from a buyer using a conventional loan, but only 30 percent would be likely to accept an offer from a buyer with an FHA or VA loan. Meanwhile, 6 percent of sellers said they would not even consider an offer from an FHA or VA buyer.

What Makes Government Loans Less Attractive to Sellers Than Conventional Financing?



Source: Lawrence Yun, Jessica Lautz, and Meredith Dunn, "2021 Loan Type Survey" (Washington, DC: National Association of Realtors Research Group, 2021), https://cdn.nar.realtor/sites/default/files/documents/Loan-Type-Survey-April-2021.pdf.
Note: FHA = Federal Housing Administration; VA = US Department of Veterans Affairs.

URBAN INSTITUTE

A new Urban Institute analysis of HMDA data from mid-2017 through May 2020 found that the FHA market share averaged 22.8 percent of all purchase loans, but dropped to 18.9 percent in the past two months. The VA share also held steady until May, averaging 11.5 percent, but has fallen to 10.3 percent in June and July.

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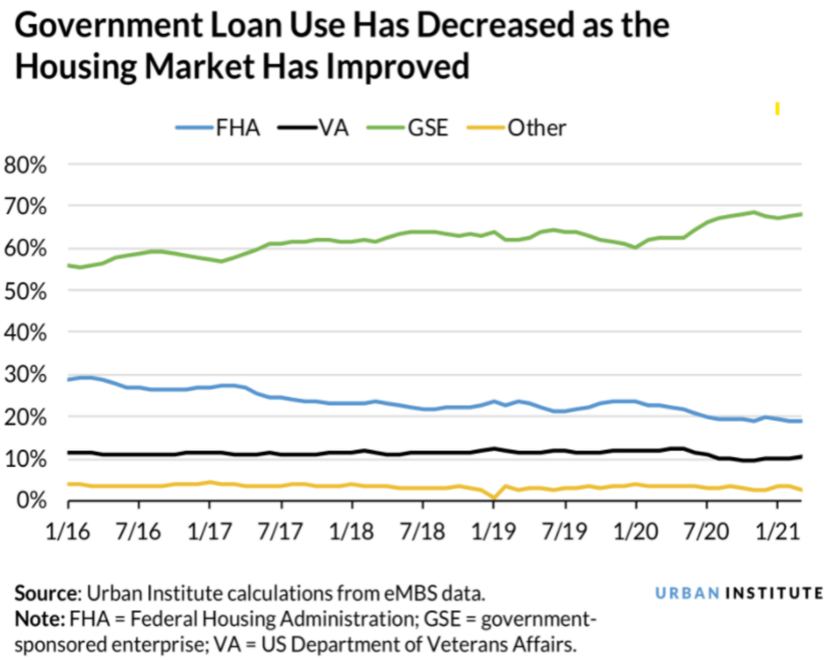
(*The FHA and VA Market Shares are Shrinking* continued)

"In a hot housing market, borrowers using FHA or VA mortgages are at a disadvantage to those using conventional mortgages. And the borrowers who disproportionately use these mortgages are the families of color who have historically been excluded from homeownership and could most benefit from today's low-interest rates," wrote UI's Laurie Goodman and Janneke Ratcliffe.



Source: [Urban Institute]

If the home is appraised for a government loan for less than the agreed-upon price, the seller must reduce the purchase price to match the appraised price or the deal cannot proceed. And if the borrower lists the home again, the appraisal stays with the home for 120 days. With a conventional loan, if the home is appraised for less than the agreed-upon price, the parties can renegotiate the price. The buyer can pay the difference between the renegotiated purchase price and appraised value. This gives the seller more flexibility if the property fails to appraise.

The Urban Institute analysts suggested that the federal government consider several steps to make the government loan process more efficient and make first-time borrowers, borrowers with less wealth, and borrowers of color more competitive. For example, the FHA and VA could more closely align their rules with those of Fannie Mae and Freddie Mac, so government loans are no longer at a disadvantage. The US Department of Housing and Urban Development (HUD) and the VA could consider either eliminating the home inspection or making it less prescriptive. Similarly, HUD and the VA could consider making appraisal requirements more flexible, using the same rules as currently apply to GSE mortgages.

“Reducing these barriers can help government borrowers gain more equal footing with conventional borrowers. It is just one of many steps that could shrink the racial homeownership gap and make the mortgage market fairer and more equitable for all borrowers,” they said.

The Inventory Crisis

Starter Home Supply Cripples Inventories

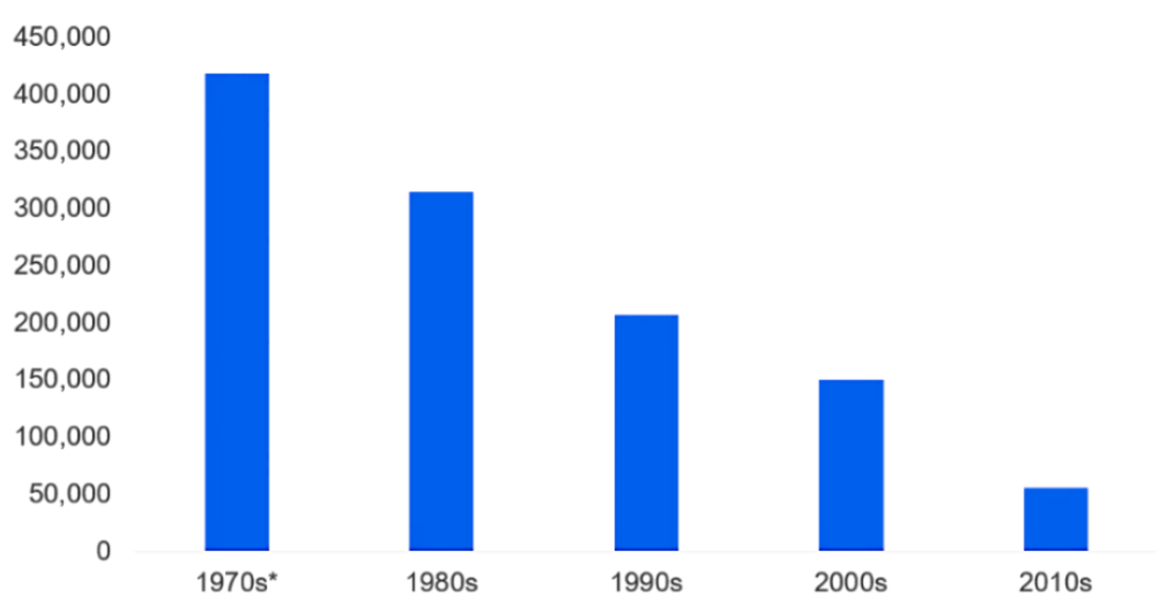
In June, more listings from sellers and a rare monthly increase in new home starts sprinkled a little water on the worse inventory drought in recent memory. The total housing inventory amounted to 1.25 million units at the end of June, up 3.3 percent from May. Sales will end the year slightly above last year's level, expects Freddie Mac's chief economist, Sam Khater, who thinks the rapid run-up in house prices may be starting to exhaust potential homebuyers.

"The one-month pause in the drought isn't nearly enough to make a dent in the nation's critical housing shortage that reached 3.8 million units at the end of last year," wrote Khater in April. "The main driver of the housing shortfall has been the long-term decline in the construction of single-family homes. That decline has resulted in a decrease in the supply of entry-level single-family homes or 'starter homes'."

Annual construction of starter homes had declined from an average of 418,000 units per year in the 1970s to only 65,000 entry-level homes last year. In 2020, only 65,000 entry-level homes were completed, but 2.38 million first-time homebuyers purchased homes.

"Not all renters looking to purchase their first home were in the market for entry-level homes; however, the large disparity illustrates the significant and rapidly widening gap between entry-level supply and demand," Khater concluded.

Figure 1: New Entry-Level Housing Supply at Five Decade Low
Number of New Homes Constructed Below 1,400 Square Feet



Source: Bureau of the Census. *Due to data limitations, represents 1976 to 1979 only

Source: Freddie Mac

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(*Starter Home Supply Cripples Inventories* continued)

"As we navigate our way through the year and get beyond the pandemic, we expect the housing supply shortage to continue to be one of the largest obstacles to inclusive economic growth in the US. Simply put, we must build more single-family entry-level housing to address this shortage, which has strong implications for the wealth, health and stability of American communities," Khater said.

The Wall Street Journal reported on August 10 that home builders are restricting sales to further fuel new home prices at a time when the median existing-home price has climbed to a record high of $363,300.

Recent housing data reflect the discrepancy between building and selling in the new home market. Housing starts, a measure of US home-building activity, climbed 29 percent in June from a year earlier, according to the Commerce Department. But sales of newly-built homes slid 19 percent in the same time frame.

"Builders are managing their waitlists of buyers in different ways. Some are selling homes first-come, first-served, while others are holding lotteries or asking buyers to submit offers above the list price," wrote the Journal's Nicole Friedman.

Minority Homeownership

Support in Congress Grows for DPA

Before Congress left Washington for its August recess, support for new federal down payment assistance was moving forward in the House of Representatives and the Senate and could become effective as soon as October 1.

On July 29, the House of Representatives approved a $50 million set-aside to fund a new federal down payment assistance program to help first-time, first-generation home buyers purchase a home. Funding for the unnamed DPA program is included in appropriations for the HOME Investment Partnerships Program (HOME).

In July, Congresswoman Maxine Waters (D-CA), who chairs the House Financial Services Committee, proposed a $100 billion down payment assistance bill to provide up to $25,000 to first-time homebuyers. Many other bills addressing first-time buyers have been introduced in Congress this year, including the tax credit plan proposed by the Biden-Harris campaign,

Senate will take up HUD Appropriations in September

The Senate Appropriations Committee will take up the FY 2022 HUD appropriations after the Senate returns on September 13. The appropriations could clear Congress by October 1, the beginning of the 2022 federal fiscal year.

On August 10, Senate Democrats released a $3.5 trillion social infrastructure financing framework that includes general support for down payment assistance within $332 billion of Housing Trust Fund funding. The Democrats' proposal would be part of an abbreviated budgetary process known as reconciliation, with the $1.2 trillion bipartisan infrastructure package passed the Senate on August 10.

First-time Buyers

Rent vs. Buy in 2021

"Should we rent or buy?" is a question at every young family's dinner table. In the gloomiest days of the housing bust a decade ago, the pro-rental lobby forecasted that a "rentorship" society would replace homeownership.

Conditions have taken a 180-degree turn since then. Today's first-time buyers know that homes won't always appreciate at a double-digit pace. The discussions continue among Millennials who face unprecedented barriers to become homeowners.

Recently Mark Fleming, chief economist at First American Research, wrote:

"I think one of the most amazing stats that I've come across in my years working as a real estate economist is really measuring the benefits of wealth creation of homeownership. You have to remember that this is a leveraged asset. You buy your home, say, with 5 percent down, effectively that's a 20-to-1 leverage ratio. Most Wall Street banks would die to be able to do 20-to-1 leverage ratios. If your home goes up by 5 percent, you've doubled your money – 100 percent gain – so the wealth-generating capacity is amazing. Just to put some real stats on this, in 2019. In the survey of consumer finances, the median homeowner had 40 times the household wealth of a renter, that's $255,000 for the owner, compared to only $6,000 for the renter. Homeownership is one of the best sources of wealth creation."

DPR Quick Takes

A new use for credit card points

First-time buyers have a new way to spend credit card points. According to Fannie Mae's August 4 seller letter, credit card reward points are now eligible assets for down payments, closing costs, and financial reserves, as long as they are converted to cash.

Pandemic increases starter home size

Home sizes rose from 2009 to 2015 but have declined since 2016 as more starter homes were developed. In the future, the National Association of Home Builders expects home size to increase once again, given a shift in consumer preferences for more space due to the increased use and roles of homes in the post-pandemic environment.

DPA comes to paradise

In late July, Maui County's Department of Housing and Human Concerns launched a down payment and closing cost assistance program that can equal up to 5 percent of the home's purchase price but not exceed $30,000. Applicants for the program for low- to above-moderate income households will be selected via a lottery drawing.

Down Payment Data

June 2021 Loan Data: Millennials and Gen Z

Median loan size	$200,589
FICO	718
LTV	88
DTI	28/37
Market Shares	CON 63 percent, FHA 31 percent, VA 1 percent

Source: ICE Mortgage Technology Millennial Tracker

June Purchase Loans

	LTV	DTI	FICO	RATE
All loans	74	24/36	743	3.22
Conventional	81	24/35	753	3.25
FHA	95	29/44	671	3.23
VA	98	26/41	722	2.92

Source: ICE Technology Origination Insight Report

About the Down Payment Report

A regular service of Down Payment Resource, The Down Payment Report collects, archives and distributes the latest news, research and trends in residential down payments, including down payment assistance programs, low down payment options, mortgage insurance and homeownership education. The Down Payment Report is researched and written by Steve Cook. Contact him at scook@commsconsulting.com.

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Contact: info@downpaymentresource.com.

Media inquiries: mharris@downpaymentresource.com