The New York Times

U.S. Lowers One Hurdle to Obtaining a Mortgage

By PATRICIA COHEN
DEC. 8, 2014

Hoping to lure more first-time home buyers into the housing market, the government on Monday detailed its plan to offer mortgages with a down payment of as little as 3 percent of the purchase price.

The proposal, first announced in October, aims to make mortgages more widely available to people who have a strong credit history but lack the ready cash for the standard 20 percent down payment.

Some critics warned about the risk of repeating the subprime mortgage fiasco and opening the door to higher defaults among home buyers lacking any substantive equity cushion in case of another downturn in the market. But federal housing officials and other experts challenged these concerns, saying the new programs include a range of safeguards, including underwriting restrictions, a requirement to buy private mortgage insurance and counseling to reduce the risk of defaults.

“These underwriting guidelines provide a responsible approach to improving access to credit while ensuring safe and sound lending practices,” Melvin L. Watt, the director of the Federal Housing Finance Agency, said in a statement.

Melvin Watt, head of the Federal Housing Finance Agency, said on Monday that he wanted to lure more first-time home buyers. Credit Isaac Brekken for The New York Times

Mr. Watt’s agency regulates Fannie Mae and Freddie Mac, the two large government-backed entities that guarantee mortgages and will be offering the new mortgage programs. While both Fannie and Freddie will require the loans to be fixed rate and to cover the borrower’s primary residence, some features differ.

Fannie Mae’s new My Community Mortgage program begins this week and is open only to first-time buyers with a minimum credit score of 620. Borrowers with Fannie-backed mortgages will be eligible to refinance with a limited amount of money that can be taken out.

Freddie Mac’s new Home Possible Advantage mortgages, which begin in March, will be available to both first-time and other qualified borrowers. In most cases, credit scores will be just one of several factors in determining a home buyer’s eligibility, a spokesman said. Refinancing, though with no cash-out, also will be available.

The programs are the latest efforts to promote homeownership after the collapse of the housing bubble, in hopes of reviving a housing industry that is still plagued by excessive foreclosures and struggling to overcome millions of owners still trapped in underwater mortgages.

Today, first-time home buyers — who are generally younger — account for just 29 percent of home sales, far below the historical rate of 40 percent, according to the National Association of Realtors. In the third quarter of this year, the Census Bureau reported recently, the nation’s seasonally adjusted homeownership rate was 64.3 percent, the lowest level in two decades.

The government’s move was applauded by the mortgage insurance industry, which expects a business increase from the new programs, and advocates for low-income families.

“We wouldn’t be putting borrowers in these loans if we were worried about their performance through stressful times,” said Rohit Gupta, chief executive of Genworth’s United States Mortgage Insurance Business and co-chairman of the U.S. Mortgage Insurers, a trade association.

The Urban Institute, a nonprofit research organization that generally supports social programs, concluded: “Those who have criticized low-down-payment lending as excessively risky should know that if the past is a guide, only a narrow group of borrowers will receive these loans, and the overall impact on default rates is likely to be negligible.”

Housing officials declined to estimate just how many people might take advantage of these new loans, but even supporters question the magnitude of the new programs.

Guy D. Cecala, chief executive and publisher of the newsletter Inside Mortgage Finance, estimated the effect would be modest, noting that first-time buyers who qualified for similar low down payment loans accounted for only 3 percent of Fannie-backed mortgages in 2013.

“It’s another tool in helping the housing market, but not a huge one,” Mr. Cecala said.

Since the borrowers must still be credit worthy, he explained, “this is not pushing the envelope.”

Diane Swonk, chief economist at Mesirow Financial in Chicago, also expressed doubt that this latest initiative would lure many new buyers, saying that the lack of demand and tight mortgage standards have been bigger hurdles than the size of the down payment.

Mark A. Calabria, an economist at the libertarian Cato Institute, was not as sanguine about the financial stability of the targeted borrowers. Given closing costs, he said, “You’re essentially underwater when you walk away from the table.”

“That is not a situation we should be trying to get people in,” he said.

To Andres Carbacho-Burgos, a senior economist at Moody’s Analytics, however, the danger of mortgage defaults generally comes from lax monitoring, not lower down payment requirements.

While sharing the view that the effect would be limited, Mr. Carbacho-Burgos said the program was nonetheless worth pursuing. “Anything that can be done to restart the first-time home buyer market is a good thing,” he said.