

Lending Policy: Navigating the New Normal of the Home Loan Market

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Purpose: The workshop will examine how changes in the financial markets have affected the underwriting policies of home mortgage lenders. By understanding these challenges, We hope to help nonprofit intermediaries develop programs designed to help create more opportunities for homebuyers.

Critical Issues: In 2009, nearly 1 million homes have gone into foreclosure; one out of every 136 U.S. households received a filing, the highest quarterly rate in records dating to January 2005. In the third quarter of 2009 alone 250,054 California homes were in some stage of the foreclosure process.

As a result of this extraordinary foreclosure activity banks and other lenders have had to rethink how they value property, originate loans, and what constitutes a credit worthy buyer. In the past, many lenders had minimal incentive to ensure that loans would be sustainable. Lenders would originate the loan and then sell it to investors in the secondary market, transferring the bulk of the risk in the process. Investor angst over the volume of foreclosures and potential loss has had the predictable effect of stifling the secondary market.

Prior to the creation of CDOs, CDSs, and other financial instruments designed to transfer risk, banks tended to use a model of lending based on the three Cs, they are: Credit (the credit worthiness of the borrower, Collateral (the quality of the underlying asset which underlies the loan), and Capacity (the ability of the borrower to repay the amount borrowed). While this model of loan underwriting tends to create higher quality, sustainable, loans it also poses some significant challenges in troubled financial times.

- Creditworthiness across the spectrum has been impacted by the current financial downturn.
- Determining the underlying value of property in a market freefall is difficult.
- Many potential borrowers are highly leveraged and are one paycheck away from financial ruin.

Anticipated Outcomes:

1. Help intermediaries understand the underlying weaknesses of loan applications before they submit them to lenders.
2. Identify ways that intermediaries can help lenders and borrowers address potential hurdles to obtaining a loan.
3. Identify ways for community-based groups to help borrowers build strong financial foundations that ensure long-term success.