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Lenders Redirect Attention to First-Time Homebuyer Segment

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San Diego Business Journal Staff

By Mark Larson

Emerging from the ashes of the mortgage crisis, mortgage lenders are shifting their business models to meet the hottest new demand: first-time homebuyers.

Brad Livingston, president and loan officer of Residential Wholesale Mortgage Inc., focuses his local shop on putting qualified first-time homebuyers in line for the best loan deals out there: federal government home loans offered by Freddie Mac, Fannie Mae or the Federal Housing Administration.

“We’re busy,” said Livingston of his North County market. “We’re steady.”

Malcolm Davies, branch owner of the mortgage lender Opes Advisors Inc., says last year, home loan refinancing kept his staff busy. But high unemployment has hurt this year’s refinance market. So Opes, too, has plugged into this year’s most promising demand.

“We’re seeing a rise in the mid-tier market,” said Davies. “2010 continues to be a very big year for first-time homebuyers.”

Craig Brown, founder and president of the mortgage bank Rancho Financial Inc. in San Diego, has adjusted to harsh market conditions for mortgage brokers by morphing his company from a mortgage brokerage to a bank. Brokers match buyers with loans from institutional banks, which underwrite and fund the loan. Mortgage bankers do their own underwriting and funding of a loan, then sell it to an institutional bank. The change has enabled Rancho Financial to streamline and keep more quality control over loan transactions.

Brown’s service shift has allowed his company to bring in more business.

He now has 60 loan officers, up from 20, to handle underwriting. He also looks at the change as getting back to basics with strong customer service in home mortgage lending. “You can’t give up customer service and expect to be successful over time,” he said.

A Whole New Ballgame

What’s the biggest difference in the mortgage industry now from past market conditions that created the subprime mortgage implosion nationwide?

“They’re lending to qualified borrowers,” said Livingston. Prospective borrowers must pass heavy scrutiny in four areas, he says: “assets, loan to value, credit score and income.”

Government home loans haven’t had much demand in San Diego historically, says Livingston. But now their offerings, along with market conditions, are making first-time homebuyers clamor for them.

The loans include provisions for down payments of 3.5 percent and 5 percent for loan value caps of $417,000 and $697,500, respectively.

For conventional loans, qualified borrowers have to come up with a 20 percent down payment, or if they have a high credit rating they can put down 10 percent if they pay for mortgage insurance.

And 30-year, fixed loan interest rates are attractive, in the high 4 percent to low 5 percent range, making for strong buying conditions. Meanwhile, and key to the whole equation, home values are down 30 percent to 40 percent.

Lending Opportunities

These days, the biggest lending market Livingston sees is for homes valued between $600,000 and $700,000.

And spurring activity now is an $8,000 federal tax credit for first-time homebuyers, which expires in April, but applies to any home purchase that closes by June 30. Repeat buyers are offered a $6,500 tax credit.

To make deals happen, Livingston says, parents are helping their kids with the down payment on a home.

Areas such as Escondido, Chula Vista, Oceanside, Pacific Beach and Vista, where new-home developments and a lot of foreclosures exist, are tough lending markets, says Livingston. But he sees plenty of stable markets in East County areas such as La Mesa where people have homes with 15 to 20 years worth of equity built up.

Real estate investors, meanwhile, are starting to look at downtown San Diego condominiums as good opportunities, he says. Investors are buying selectively, looking for high yields on rental property.

“They’re more sophisticated, looking at more of a long-term deal instead of flipping it,” said Livingston.

Overall, he adds, “Things that are selling are priced well and they show well. It’s a buyer’s market. They’re very savvy. They want value. They want to see they’re making a smart purchase.”

Rough Road Ahead

Despite the signs of a recovering market, Livingston isn’t overly enthusiastic about it. There is still a rough economy out there.

“We’re not out of the woods yet,” he said. “People don’t buy houses if they’re unemployed.”

Davies of Opes Advisors sees two types of customers these days. There are first-time homebuyers, who are relatively easy to underwrite if they qualify as viable wage earners. But it takes a lot of scrutiny to see if they qualify.

Then there are the self-employed borrowers and entrepreneurs looking for loans. New regulations require an extreme amount of loan qualifying documentation on these clients. And these cases take time to process, says Davies.

“We go through with a fine-tooth comb to see if they qualify in the marketplace,” he said.

Clients are told upfront that vetting their financials is likely to be lengthy and vigorous and to be prepared for it. That, he says, goes a long way toward minimizing angst during the process.

Even well-qualified investors get a detailed financial review on deals, and Davies adds, “They’re shocked at how much information we have to collect from them.”

Domino Effect

All that scrutiny has lowered the number of people who can qualify as buyers, and that, says Davies, has brought down property values.

Those that pass the test, however, get a loan that has true merit and, unlike what was common only a few short years ago, isn't based on smoke and mirrors.

"The client will reap the rewards of a solid underwriting," he said. "They'll live in a stable neighborhood that isn't going to have foreclosures."

His company has underwriters updated on regulations on a weekly basis, because rules change that often.

"You need to adapt to it," he said. "You can't be frustrated. If we understand the reasons behind them, we won't just ask 'Why?' "

All that change, he says, means "We have to work three times as hard to get half as much" as in a typical market.

He expects interest rates will go up during the next 12 months, and notes that even an incremental rise can chill the buying market.

Brown of Rancho Financial says the guidelines for Fannie Mae, Freddie Mac and FHA loans aren't complicated.

"They're really not that hard to deal with," he said. "The problem is there is a very uneven way of applying them."

Lenders tend to have varying risk guidelines in documenting loan applicants to cover themselves, he says, resulting in different rates, all because they fear having to repurchase the loans they're doing.

Because of that bit of vetting overkill, says Brown, "A lot of loans get turned down that otherwise would have met Fannie Mae guidelines."

But Brown says these overreactions will calm down over time. He saw a similar scenario in the early '90s. "We thought we were in a free fall at that time as well." He figures some sort of normality will come once the home loan foreclosure crisis settles down, which he sees happening in the next 12 months.

Of the bunker mentality of large mortgage lenders, he adds, "It just can't continue at this same level."

Mark Larson is a freelance writer for the Business Journal.
