Industry at Loggerheads Over Need for More FHA Premium Cuts

By Brian Collins
January 19, 2016

WASHINGTON – As the Obama administration prepares to release its final budget, banking and mortgage groups are split on whether it should include another reduction in the premiums the Federal Housing Administration charges on single-family loans.

In one corner are groups like the Community Home Lenders Association and the major credit union groups, which are hoping the administration will further cut premiums after a reduction a year ago.

The Department of Housing and Urban Development cut the FHA's annual premium by half a percentage point to 85 basis points at that time, but the agency's fortunes have rebounded even faster than expected since then, fueling interest in a further cut.

"The Community Home Lenders Association is writing to request that the administration include a reduction in FHA annual premiums in its FY 2017 Budget, down to a level of 0.55% for most loans," Scott Olson, the executive director of the Community Home Lenders Association, wrote in a letter last week to the Office of Management and Budget. The OMB is set to release the 2017 fiscal year budget on Feb. 9.

But in the other corner are industry players like the Mortgage Bankers Association, which warns that a cut now could be a bad idea for economic and political reasons. The agency's ratio of reserves to guaranteed loans jumped to 2.1% as of Sept. 30, up from 0.4% a year earlier and just above the 2% statutory minimum.

David Stevens, the head of the MBA, warned that the political fallout if the fund went below the 2% level again could be significant.

"Members of the House Financial Services Committee would have a field day declaring once again that FHA mismanaged the program," said Stevens, a former FHA commissioner.

The most recent projection said the capital ratio of the agency's forward book (guaranteed loans that are not reverse mortgages) is 1.6%, but Stevens said it should be higher before the agency enacts another cut.

"We can't risk the program until it is clear that the forward book on its own is well above the 2% threshold," Stevens said.

Stevens is worried the volatility in the FHA's reverse mortgage program could push the overall ratio below 2% again.

Other groups are also skeptical of a cut.

"We are more concerned about maintaining the health of the FHA Mutual Mortgage Fund," said Ron Haynie, senior vice president of the Independent Community Bankers of America.

But the Community Home Lenders Association and the credit union groups said that now is the time for a cut considering the FHA's recent turn around. Olson noted that last year's premium cut not only increased loan volume – which rose 50% -- but helped boost the FHA's strong financial performance.

Credit quality has also improved. The serious-delinquency rate fell to 5.79% in October, a seven-year low.

In an interview, Olson argued that a further reduction in the annual premium would make FHA-insured loans more affordable for first-time homebuyers.

"You don't want to wait until it is clear you have completely recovered to start making these sorts of affordability considerations. We think you can accomplish both in the same time," Olson said.

The Credit Union National Association and the National Association of Federal Credit Unions agree a premium reduction makes sense.

"CUNA supports the reduction in the FHA annual premiums," said Andy Price, senior director of advocacy and counsel at CUNA. "Anything the FHA can do to make mortgages easier and more affordable for first-time homebuyers is certainly welcome."

Curt Long, NAFCU's chief economist, said that "the housing market is still struggling as many Americans, particularly first-time buyers, simply cannot afford the cost of home ownership. Cutting FHA premiums bolsters the housing market and would be welcomed by credit unions as they continue to serve their 102 million member-owners."

The American Bankers Association, meanwhile, appears caught in the middle.

"Not too long ago there were concerns about the stability of the FHA insurance fund, but now it looks like it is getting more stable and healthy," said Joe Pigg, a senior vice president at the ABA.

That naturally raises the question about when the FHA should reduce its fees.

But the ABA would not be "leading the charge" for a reduction, Pigg said. "We would only weigh in if it reached a point where we thought they should have acted already."

For its part, the FHA appears to be leaning against a further cut for now. Edward Golding, the FHA's deputy principal assistant, has signaled a cut is not yet in the works.

"I support the direction that Ed Golding is taking, which is holding off on an premium reduction until the fund is not just over the line but it has clear, sustainable capital above the 2% statutory obligation," Stevens said Thursday.

Some observers say that the administration is reluctant to make another cut in the short term but that it might consider pricing changes closer to the end of the year.

Isaac Boltansky, a research analyst with Compass Point Research & Trading, said that it's doubtful there will be another premium cut this year but that the chances have improved slightly.

"In terms of pricing, we are increasing our odds for another FHA pricing change in 2015 from 20% to 30% given an increase in chatter regarding the potential for changes to the FHA's cancelability policy," Boltansky wrote in a Jan. 13 note to clients.

Others agreed that a move in the latter half of the year was more likely.

"I do think that an MIP reduction is merited this year, but I would be surprised if anything was imminent," said Brian Chappelle, co-founder of the consulting firm Potomac Partners in Washington.