

Federal Assistance Needed to Keep Mortgage Capital Flowing through Warehouse Lines of Credit

MBA RECOMMENDS

In order to provide much needed capacity in the mortgage market to reach borrowers for purchase and refinance transactions, Congress and the administration should take steps to help maintain existing lines of warehouse credit and create new lines of warehouse lending by providing a short-term (i.e. 12–24 months) federal guarantee of warehouse lines that are collateralized by Fannie Mae, Freddie Mac, FHA, VA and RHS-eligible mortgages that are held for sale by mortgage lenders. This action by the federal government is urgently needed to maintain the mortgage funding structure borrowers depend upon, especially borrowers who rely on independent, non-depository lenders. In addition to this wide-impact solution, other steps should be taken, including modifying the present risk-based capital treatment of warehouse loans to facilitate the expansion of warehouse lending.

WHAT IS WAREHOUSE LENDING?

Warehouse lending is a short-term revolving line of credit provided to a mortgage banking company to fund the closing of mortgages from the closing table to sale in the secondary market. The mortgage note is used as collateral for interim financing until the mortgage is sold and delivered to the permanent investor. Mortgage bankers draw upon the line of credit to fund a mortgage at closing or to purchase a closed loan from another originator. The line of credit is paid off when the loan is sold to the end investor. Warehouse lending contributes to the financial capacity the industry provides for originating loans for first-time homebuyers; refinancing troubled borrowers into new mortgages; assisting other borrowers in securing credit for residential mortgage transactions; and originating loans for the purchase, refinance or repositioning of rental properties.

BACKGROUND

Recently, the amount of warehouse lending has declined significantly, and this trend is a present and growing danger to a source of capital for many mortgage lenders and borrowers, especially those wanting to refinance.

Warehouse lenders going out of business, terminating, or adding restrictions to their warehouse lines of credit are causing independent (non-depository) mortgage lenders to struggle to maintain their ability to serve borrowers. Warehouse lenders serve as a crucial short term funding source for mortgage bankers, specifically those that are non-depository institutions, which help maintain adequate capacity for all forms of mortgage originations, including home purchases, refinance and modifications for troubled borrowers, and other transactions. According to *National Mortgage News*, there were approximately 90 warehouse lenders in 2007; today there are approximately 40 warehouse lenders.

Warehouse lending capacity has declined dramatically – from over \$200 billion in 2007 to approximately \$20 to \$25 billion in 2008, a decline exceeding 85 percent. For the originator that depends solely on warehouse lines of credit, this reduction could extinguish its lending business and adversely impact the borrowers in its market, stifling the real estate recovery before it gets off the ground.

Recently, several commercial banks have purchased other institutions that are active in the warehouse lending business. The future of warehouse business appears

uncertain because many banks have pulled-back on warehouse lines, ceased to issue new lines or stopped increasing existing lines, increased pricing and restricted terms have closed down lines altogether. These actions have left many non-depository lenders without adequate and viable sources of capital.

Other warehouse lenders may not continue to extend credit to lenders because of the perceived risk, headline risk or otherwise, of products associated with mortgages, despite the fact that mortgage underwriting is extremely rigorous and conservative today. Mortgage bankers that rely on warehouse lines of credit will be unable to maintain their businesses and cannot serve their local communities if their sources of warehouse lines are not maintained. MBA believes the federal government could be helpful in a variety of ways in keeping these lines of credit available and functioning effectively.

SOLUTIONS

Because funding for warehouse lending has dried up at such a rapid pace, long term plans, such as creating a mechanism at the Federal Home Loan Banks to provide warehouse funds, would not address quickly enough what is becoming a crisis in which time is running out. Below are solutions MBA believes are high impact, viable and can be implemented quickly:

Immediate Solution

Congress and the administration should take steps to help maintain existing lines of warehouse credit and create new lines of warehouse lending by providing a short-term (i.e. 12–24 months, should be available until warehouse market liquidity normalizes) federal guarantee of warehouse lines that are collateralized by Fannie Mae, Freddie Mac, FHA,

VA and RHS-eligible mortgages that are held for sale by mortgage lenders. This would help warehouse lenders to be more willing to allocate greater financial resources to warehouse lending because of this government backstop.

Narrow Impact Solution

The federal banking regulators, including the Federal Reserve, the OTS and OCC, and FDIC require warehouse lenders to treat warehouse lines of credit as 100 percent risk rated assets, along with other commercial loan exposures. MBA believes that warehouse lines of credit, if properly managed, have risks comparable to directly originated conventional and government-insured mortgage exposures and in the final few days in the warehouse process, the risk is comparable to holding a government or government agency mortgage-backed security (MBS). MBA recommends that the risk-based capital rules be modified to more properly risk-weight these assets.

SOLUTION LIMITATION

Although this proposal provides a warehouse capacity shortage solution specifically tailored for loans with actual or effective government guarantees (GSE, FHA, VA and RHS-eligible residential and multifamily mortgages), it is not an appropriate solution for non-government guaranteed private label residential, commercial and multifamily loans. In order to address this issue, MBA will work with Congress, Treasury and the administration to craft solutions that provide for increased warehouse lines of credit capacity for private label residential, commercial, and multifamily loans. By addressing both government guaranteed and private label loan categories, a complete solution to the capacity shortage for warehouse lines of credit can be developed.



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