Thanks to Investors, the Mortgage Business Is Shrinking

lending industry update credit risk

Summary: The US housing market has been red-hot for a good while. However, overvalued home prices, rising interest rates, and the growing number of home purchases by private equity firms mean that, for many financial institutions, the traditional mortgage business is shrinking. CFIs that want to compete in this space should market specifically to traditional homebuyers, and all CFIs should be aware of how this will impact the makeup of the communities they serve.

Famous Broadway rock musical "Rent" portrays a group of friends struggling to maintain housing as their landlord reneges on a previous deal, and demands the past year's rent. But the full scope of issues the characters are grappling with goes much deeper. Featuring a public health crisis, discrimination, loss, and employment struggles, the setting draws many parallels with the issues faced by today's minority communities in the wake of COVID-19, especially regarding the economy and the housing market. These factors ultimately impact the community financial institutions (CFIs) who service these neighborhoods in a negative way, despite the market's outward look of soaring prices and booming sales. Much like the characters in "Rent," who face hidden inner struggles, looks can be deceiving, and it will take resilience to persist.

The US housing market has climbed in both value and number of homes sold in the past two years. Home sales are projected to reach 7MM in 2022 . Housing starts were up 3.9% from March 2021 to March 2022, leaving a deficit of 2.5MM housing units . A strong seller's market saw the median price of existing homes go from a high of $296,700 in 2020 to $390,500 by July 2021, fueled by historically low interest rates and pandemic-related consumer needs for more space at home.

Looking at who exactly is purchasing these homes, a more complex story emerges. According to Redfin, investors were securing 15% of homes in major metropolitan areas. In some cities, it was much higher including Charlotte, NC and Atlanta, GA, with 25%.

Some investors rehabilitate and sell homes to other buyers, who might be investors or new residents; others simply rent out their purchases, as rent prices have also become very inflated. What this all boils down to is fewer home sales to actual residents and more homes than ever being grabbed up by companies who are looking to profit from the booming housing market.

Investors target lower-priced minority neighborhoods

Investors are particularly interested in neighborhoods where a majority of residents are black, and housing prices have historically been lower than in non-minority neighborhoods. According to the Washington Post, 30% of investor home purchases in 2021 were in majority black neighborhoods, compared with 12% overall.

That statistic is part of a worrying trend. In 2010, investors bought 14% of homes sold in black neighborhoods, compared with 7% overall . The impact for those neighborhoods and residents is that they are being priced out of their local market and unable to take advantage of high selling prices. They also can't afford to refinance at these rates, meaning fewer sales to traditional homebuyers in those communities.

The trend is toward fewer mortgages

The growing proportion of homes bought by investors has several impacts on CFIs as well. Here’s a look at the most crucial ones:

- **CFIs will have fewer mortgage loans.** That, is in part, because the investors who buy property to flip or rent often don’t need traditional mortgages. They’re either paying cash or securing a short-bridge loan to get them through rehab and to resale.
- **Investors are driving homebuyers out of affordable areas.** Investors’ concentration on affordable neighborhoods drives prices upward in those communities. As a result, fewer residents can afford to buy homes in the areas they already live in, and prospective residents may be priced out of the market. Higher rents may force out tenants, too, who will likely move out of the area and leave their CFI. This changes the overall makeup of the communities CFIs serve.
- **First-time homebuyers are hitting pause.** According to Nadia Evangelou, senior economist with the National Association of Realtors, first-time homebuyers will shop for a new home this year, but will be unable to purchase one. This group totals over 2.5MM people.
- **Rising interest rates may halt hesitant purchasers.** Higher interest rates translates into a potential homebuyer from being able to afford less of a home. On July 25 of this year, a 30Y fixed-rate mortgage might have carried an interest rate of 5.33%. In 2021, the average rate was 2.96%, which was the lowest annual average in the past 30Ys. This could be one reason behind a rise in homebuyers backing out of deals at the last second.

Although the outlook for CFIs who rely on mortgages is still up in the air, being aware of how investors are impacting the real estate market can fill in a big piece of the puzzle. CFIs who have a pulse on investor impact in their community can help ease potential homebuyers’ worries by helping them plan ahead for a future home purchase. Rather than convincing tentative homebuyers to make a move that could result in higher risk for your CFI, present them with investment options to grow their down payment, while they wait for the right time to make a purchase. This considerate, patient approach will benefit both you and your future mortgage customers in the long run.

PCBB PODCAST: EXCITING, NEW & INFORMATIVE

ECONOMY & RATES

Rates As Of: 08/29/2022 05:47AM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	2.89	0.48	2.83
6M	3.26	0.35	3.07
1Y	3.37	0.44	2.98
2Y	3.43	0.55	2.70
5Y	3.25	0.58	1.99
10Y	3.09	0.44	1.58
30Y	3.24	0.23	1.33

FF Market	FF Disc	IORB
2.33	2.50	2.40
SOFR	**Prime**	**OBFR**
2.28	5.50	2.32