MBA

MORTGAGE BANKERS ASSOCIATION

July 14, 2015

Alfred Pollard
General Counsel
Federal Housing Finance Agency
400 7th St., SW
Washington, D.C. 20024

**No: 2015-N-03 -** Comment on FHFA's Request for Input Re: Notice of Establishment of Housing Price Index

Dear Mr. Pollard:

On May 21, 2015, FHFA published a request for input (the Request) on its proposal to establish and maintain a method for assessing the national average single-family house price for use in adjusting the conforming loan limits of Fannie Mae and Freddie Mac (the GSEs). In the Request, FHFA stated its intent to use the FHFA "expanded-data" house price index (HPI) to adjust the conforming loan limit.

MBA appreciates the opportunity to provide the following general comments:

- FHFA's review regarding alternative indexes is thorough, and the choice of the expanded-data HPI seems sensible, and should provide an accurate read of home price changes for these purposes.

- MBA would urge FHFA to consider steps to maximize transparency with respect to the calculation of the loan limits and all intermediate statistical results. The approach taken, while well-justified in terms of methodology, is not fully transparent because it relies upon non-public data and a relatively complex statistical procedure.

- Although it has not been the case for much of the existence of the GSEs, currently jumbo rates continue to run even with or below conforming rates on 30-year fixed loans, according to MBA and other surveys. Some might view this as diminishing the importance of determining conforming eligibility. However, that would be a mistake as other benefits beyond the mortgage rate accrue to GSE eligible loans. In particular, GSE loans benefit from the QM "patch," while jumbo loans face a binding debt-to-income (DTI) constraint.

More specific comments and questions are addressed below.

## Background

Under the Housing and Economic Recovery Act of 2008 (HERA), FHFA is required to establish and maintain an HPI for use in adjusting the conforming loan limits of the Enterprises. The change in the index determines the extent to which the baseline national loan limit is changed. The current national limit, $417,000, has been in place since before the crisis due to the practice of holding the limit unchanged in the event of a home price decline. Under any index chosen, the limits would not increase again until home prices exceed their pre-crisis peak. Given the strong growth in home prices in recent years, we are approaching prior peaks, at which point the limits would need to be adjusted.

Loans that meet the conforming limits are eligible for purchase or securitization by the GSEs. Loans above this level are ineligible, and are likely to be held on balance sheet or potentially securitized through a private-label issuance.

## General Comments and Questions

### *Alternative Benchmarks*

For many years, the benchmark for adjusting the baseline loan limit was the average home price as captured in the Federal Housing Finance Board's Monthly Interest Rate Survey. This survey utilizes a relatively small sample of conventional purchase loans, and does not control for the composition of homes that sell in any particular period. Most analysts prefer to track repeat sales indexes, which do control for the quality of homes that are transacting.

FHFA examined several alternative home price indexes in this analysis, including traditional FHFA indexes (which utilize data only from the GSEs), the FHFA expanded data index (which incorporates transactions not financed by the GSEs, in particular Federal Housing Administration (FHA)-endorsed loans and homes whose transactions have been recorded at various county recorder offices through the country), other repeat sales indexes from private data providers, and median price series.

In evaluating which index to use, FHFA considered a number of factors. The most important factor was whether price changes reflected in the measure would closely match changes in the U.S. average home price. By matching the change in the US average, the GSE's share of the market should remain unchanged over time, which is consistent with FHFA's goal of maintaining their role to provide liquidity to the conforming conventional market. MBA anticipates that legislative GSE reform would prompt a further discussion regarding the appropriate level of the conforming loan limit. However, accurately gauging the change is a methodological discussion, so this is the right goal.

In addition to accuracy, FHFA also highlights that data and methodological transparency are important goals. MBA agrees, and highlights this goal further in our discussion below.

We appreciate that all of the indexes considered by FHFA report a similar evolution of home prices since 2007. However, historically the greatest discrepancies appear across these indexes when prices reach an inflection point, which can influence the types of transactions that occur, and thereby lead to different samples underlying each of these indexes. The high post-crisis correlation across these measures may not necessarily be maintained in the years ahead.

In the analysis, FHFA considers the question of whether or not to include distressed sales in the index database, and decides to do so. This is an important distinction that likely bears close observation over time. One question to ask would be whether any of the distressed sales are bulk transactions to institutional buyers rather than individuals, and whether this difference impacts the observed price change. While these issues are important, however, it is unlikely to make a material difference in the loan limit calculation for the foreseeable future.

Going forward, it is sensible to choose the index that has the broadest sample in order to minimize the risk that the index would be biased due to an insufficient number or unrepresentative mix of transactions entering the sample. FHFA's proposal to use the expanded data index is the right one, as it would not be skewed in the event that the conventional conforming market behaves differently from the broader US housing market.

***Importance of Transparency***

It is important for FHFA to recognize that changes to the conforming loan limit are a major undertaking across the industry. Every lender and many service providers make changes to their systems, and must do so rapidly as applications taken late in the year are likely to be originated in the following year in which the new limits apply. For these reasons, the industry needs a process which is clear, transparent, and predictable. FHFA's choice of an appropriate methodology and a broad sample minimizes the risks that noise from a single month of data could skew the index calculation. However, the choice to use non-public data that is combined with GSE data, and the choice of a commonly used, but admittedly complex statistical procedure for index calculation, will require FHFA to consistently and clearly communicate with the market regarding trends in these data and any potential changes to the sample. For example, FHFA could regularly report on the proportion of the sample that derives from GSE, FHA, and other data sources, and also the proportion that are distressed transactions or from bulk rather than individual sales.

In the notice, FHFA does commit to notify the public of any data enhancements. This is critical. It would also be helpful to regularly publish monthly summary statistics and trends from the expanded data set to increase clarity and the market's ability to more accurately anticipate the new loan in limit in the period immediately prior to the change date. MBA and other forecasters may choose to begin forecasting the expanded data HPI if sufficient historical information is made available.

With respect to the methodology, as highlighted in the notice, a complication with repeat sales measures as typically implemented is that the entire historical series is re-estimated each time the index is calculated. Although FHFA notes that, for the purposes of loan limit calculation, they will rely upon only the most recent estimate for each time period, the potential for volatility in historical values could lead to confusion among some market participants.

FHFA should further explore the option of constraining index values, at least for some portion of the index history. Regardless, FHFA should be very careful to highlight and explain any significant index revisions as they occur, and the potential they have for changing the conforming loan limit calculation.

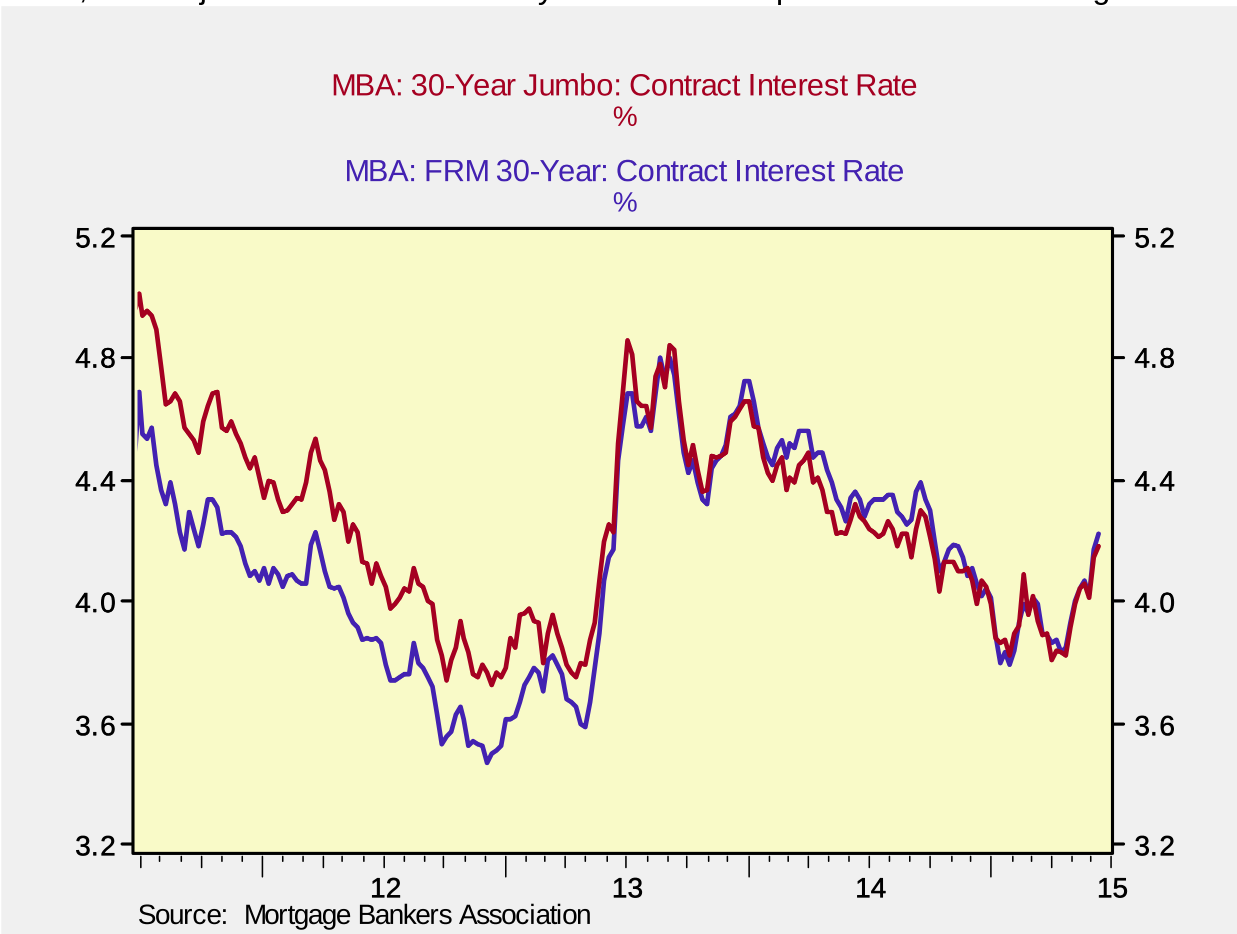
***Ongoing Importance of Conforming Status***

Over the past few decades, it was typical for 30-year fixed conforming rates to be 25 basis points or more below 30-year fixed jumbo rates. However, for a number of reasons, beginning in 2013, jumbo rates have typically been even with or lower than conforming rates, according to data from MBA and other surveys. Some might view this as diminishing the importance of determining conforming eligibility.

However, that interpretation would be a mistake as other benefits beyond the mortgage rate accrue to GSE eligible loans. In particular, GSE loans benefit from the QM "patch". Although Fannie Mae and Freddie Mac are required to adhere to the product, documentation, and points and fees limitations of the CFPB's QM rule, for the seven years following implementation or until the GSEs exit conservatorship, a GSE underwriting approval substitutes for the 43 percent DTI limit that is part of the rule. This "patch" is quite important, as it allows borrowers to compensate for a higher DTI with other factors such as down payment or credit history.

For jumbo loans, the 43 percent threshold can be a binding DTI constraint. This is particularly ironic as what is effectively a stricter standard is being applied to high income, high wealth jumbo borrowers, who nevertheless have ample residual income even if they have a high DTI. MBA has advocated for exempting jumbo borrowers from the ATR/QM rule.

The relevance here is that changes to the conforming limit establish the portion of the market that benefits from the "patch" while it is in place. This is critical for access to credit, even if jumbo rates are currently more than competitive with conforming rates.




## Conclusion

MBA appreciates FHFA's careful review regarding the index to be used for calculating changes to the conforming loan limit. FHFA's decisions in this respect seem sensible, and should provide an accurate read of home price changes for these purposes.

It is important that FHFA focus on maintaining transparency with respect to the calculation of the loan limits and all intermediate statistical results. The approach taken, while well-justified in terms of methodology, is not fully transparent because it relies upon non-public data and a relatively complex statistical procedure.

Conforming loans continue to benefit from additional flexibilities and liquidity that are not available with loans above the conforming limit. For these reasons, an accurate and transparent calculation of the conforming loan limit will remain very important to the industry going forward.

Any questions on MBA's response should be addressed to Mike Fratantoni at (202) 557-2935 or MFratantoni@mba.org.

Sincerely,

David H. Stevens
President and Chief Executive Officer