



Federal Financial Analytics, Inc.

PETROU URGES CAUTION ON FHA ZERO DOWNPAYMENT LOANS

“In my opinion, the FHA must make every effort to avoid placing first-time homebuyers – especially low- and moderate-income ones – in a position where their hopes of moving to accept a new job or live close to family are dashed solely because of a zero-downpayment mortgage taken out years before.”

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WASHINGTON, D.C. – In testimony today before the House Financial Services Housing Subcommittee, Federal Financial Analytics’ managing partner Basil N. Petrou outlined a number of potential risks possible if Congress acts on H.R. 3755, legislation to implement the Administration’s proposed new zero-downpayment FHA program. Petrou spoke in strong support of the home-ownership goals behind the proposal, especially with regard to under-served low-income and minority borrowers. He noted, however, that zero-downpayment loans are seen in the private sector as a high-risk proposition, and these risks can be compounded if the FHA does not take steps to protect vulnerable borrowers.

“FHA entry into zero downpayment loans must be carefully structured to prevent risk to borrowers, communities, and the rest of the FHA Mutual Mortgage Insurance fund,” Petrou said. “HUD should consider limits beyond those currently proposed for zero downpayment loans. These could

include targeting the program to low-and moderate-income borrowers, reliance only on proven FHA lenders, and increased sampling.”

Petrou’s testimony noted that borrowers who take out a zero-downpayment loan actually have still higher loan-to-value (LTV) ratios the day they close, with these LTVs reaching 103%, 105% or even higher because of all the costs involved in taking out a mortgage (including the FHA’s own up-front premium). Thus, these borrowers are at particular risk from faulty appraisals and adverse personal or housing market events. If these very high-LTV loans are concentrated in low- and moderate-income neighborhoods, a spurt in foreclosures that results in neighborhood distress will exacerbate, not cure, the home-ownership problems in the communities the proposal rightly hopes to help.

Petrou’s testimony is attached.

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