



Mortgage Supply & Homeownership

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Outline Of Remarks

- I. The Literature – A Tale of 4 Model Types
- II. Is Homeownership the Mortgage Problem
- III. Who needs more Mortgage Debt?
- IV. Is Government Part of the Problem?
- V. Needed Changes in Mortgage Supply



Model #1- Simple Static

- ◆ Use data on current renters or low income owners
- ◆ Use house value = 50% of area median
- ◆ Ask how many can't qualify for a mortgage to purchase the target house value
- ◆ Data problems mean credit score omitted
- ◆ Income is often a problem for ownership



Model #2 – Complex Static

- ◆ 1. Consider joint choice of housing & finance
- ◆ 2. Downpayment constraints are more important than payment-to-income ratios
- ◆ 3. FHA is most important– the “FHA” wedge
- ◆ 4. In mortgage choice equations, credit constrained households choose FHA
- ◆ 5. FHA share rises during local downturns



Model #3 Short Run Dynamic

- ◆ 1. Focus on household behavior just before homeownership
- ◆ 2. First time owners increase saving and income before attempting to buy
- ◆ 3. Households try to remove downpayment, payment to income and credit constraints
- ◆ 4. Lower interest rates and downpayments may only change the timing of homeownership



Model #4 Long Run Dynamics

- ◆ 1. What is the effect of variation in mortgage terms on lifetime homeownership?
- ◆ 2. International evidence favors a relation between mortgage supply and ownership
- ◆ 3. No effect using US alone
- ◆ 4. Informal evidence from higher FHA premiums during the 1990's: no effect



Is Homeownership the Mortgage Problem?

- ◆ 1. Recent buyers have little housing equity
- ◆ 2. 30% of owners have no mortgage
- ◆ 3. Median owner < 50 has only housing equity and government-insured assets
- ◆ 4. “Burning the mortgage” is a major goal
- ◆ 5. Conclusion: the problem is that older owners have too little mortgage debt!



Who needs more Mortgage Debt?

- ◆ 1. New owners are highly leveraged
- ◆ 2. Older owners have too little mortgage debt
- ◆ 3. The average owner is poorly diversified
- ◆ 4. The housing equity “trap” catches many
 - A. Banks only lend when you don’t need \$
 - B. Lose your job and you can’t refinance
 - C. Subprime lenders fill the gap from the trap!



Is the Government Part of the Problem?

- ◆ 1. Government encourages over-investment in housing equity
 - HOEPA says “equity stripping” is evil
 - Economically marginal households are encouraged to use prepayment to build wealth – making them vulnerable to the equity trap
- ◆ 2. FHA is not run as an experiment in high risk lending.
- ◆ Banking legislation prevents use of credit scores in research



Needed Changes: Government

- ◆ 1. Stop promoting homeownership for marginal credit risks
- ◆ 2. Encourage households to diversify
- ◆ 3. Promote the reverse annuity mortgage
- ◆ 4. Use FHA as an experiment in mortgage lending
- ◆ 5. Promote research into creditworthiness



Needed Changes: Private Sector

- ◆ 1. Design mortgage instruments for owners who now have no mortgage
- ◆ 2. Allow borrowers to miss payments, access equity automatically
- ◆ 3. Stop pushing the 30-year self-amortizing dinosaur
- ◆ 4. Optimal mortgages should consider the local housing market conditions – challenge for GSE's