

# Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund

U.S. Department of Housing and Urban Development

November 12, 2009





## Secretary's Foreword

I am pleased to present to the Congress this annual report on the financial status of the Federal Housing Administration (FHA) Mutual Mortgage Insurance Fund. FHA is providing vital support to our national housing market during the most stressful economic conditions since the Great Depression. The role of FHA in supporting safe and sustainable homeownership opportunities to American families increased as conventional sources of mortgage credit became more and more restricted in 2008 and 2009. FHA and Ginnie Mae are fulfilling the role expected of them during this critical time in our nation's history. I am proud of the work done by the dedicated professionals within these two organizations. They represent the best in public service and I am proud to be at HUD and to work with them.

This report transmits results of the FY 2009 actuarial study of the Mutual Mortgage Insurance Fund. The analysis has been performed by independent third-party contractors based on professional actuarial standards. In addition, as a part of the annual audit of FHA's financial statements, the models developed by these contractors are reviewed by the auditing firm hired by the HUD Inspector General.

This year, for the first time, we have added an actuarial study of the FHA reverse mortgage, or HECM, program, to the principal study of standard FHA single-family insurance programs supported by the Fund. This is because the Housing and Economic Recovery Act of 2008 added the HECM program to the MMI Fund family of programs, starting with FY 2009 insurance commitments.

The FHA single-family insured portfolio is experiencing high levels of stress resulting from declining property values and increased levels of income and job loss. The 2005 – 2008 books of business, in particular, have elevated delinquency rates and are anticipated to have high claim

rates as they continue to season. The independent actuarial studies are important for assisting HUD in establishing loss reserves to cover the potential costs of those future insurance claims. Actual loss reserve adjustments will be made in consultation with the Office of Management and Budget, as part of the annual budget re-estimation process, but the foundations for those adjustments come from the actuarial studies presented here.

In the meantime, the need to reserve more funds for anticipated claim costs on the current portfolio of insured loans results in a decrease in the measured capital ratio. The actuary's study concludes that, for the first time since 1994, the capital ratio has fallen below the required two-percent level. In several important steps to address risk, FHA Commissioner Stevens has already put in place a number of underwriting changes and appointed a Chief Risk Officer whose sole charge is understanding and addressing risk. We will continue to monitor patterns of delinquency and default, along with broader economic conditions, to alert us to any additional actions that need to be taken to protect the financial soundness of the FHA MMI Fund programs.

A handwritten signature in black ink, appearing to read 'Shaun Donovan', is positioned above the typed name and title.

Shaun Donovan  
Secretary  
United States Department of Housing and Urban Development

## Introduction

### FHA Today

The Federal Housing Administration (FHA) finds itself in a unique position in today's housing market. FHA was largely shut-out of the mortgage market during the boom years of 2003-2007, but has now emerged as a primary source of credit guarantees both for home buyers and for homeowners seeking to refinance into lower-cost and safer mortgage products. In the fiscal year just ended (2009), FHA guaranteed more than \$360 billion in single-family mortgages. That represents a 75-percent increase over FY 2008 activity, and more than four times the volume of insurance commitments made in FY 2007. (See Table 1.)

The growth of new insurance activity in FY 2009 was the result of two primary factors. First was the significant withdrawal of capital in the conventional mortgage market in 2008. That occurred as existing capital was being reserved for current and expected losses on outstanding businesses. It became very difficult to raise capital for new credit guarantees as long as investors would also be at risk for the outstanding loan portfolios.<sup>1</sup> Private mortgage insurers are working today to legally separate outstanding business from new business in order to raise new capital and increase their market penetration in 2010.

The second factor leading to growth of FHA volumes in FY 2009 was an increase in refinance activity. That increase followed a drop in mortgage interest rates from around 6.5 percent in 2008 to close to 5 percent in 2009.<sup>2</sup> FHA is attracting into its refinance program both homeowners who previously had conventional financing, and FHA-insured homeowners looking to lower their monthly payments. The average drop in monthly payments in FY 2009, for existing FHA-insured borrowers taking advantage of the streamline refinance option, was over \$130.<sup>3</sup>

Both of these factors resulted in an increase in the underwriting quality of the FY2009 book-of-business, when compared with earlier years. Borrowers in FY 2009 had higher incomes, higher credit scores, and lower monthly payment burdens. (See Tables 2a and 2b.) An additional factor leading to a higher-quality book in FY 2009 was elimination of the option for using funds from property sellers, through nonprofit conduits, to pay homebuyer downpayments. The Congress eliminated that option in the Housing and Economic Recovery Act of 2008, which led to the ending of any measurable amounts of insurance commitments on that business by January 2009.<sup>4</sup>

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<sup>1</sup> See, Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, Glenn B. Canner, and Christa N. Gibbs, "The 2008 HMDA Data: The Mortgage Market during a Turbulent Year," *Federal Reserve Bulletin*, forthcoming, vol. 95, <http://www.federalreserve.gov/pubs/bulletin/2009/pdf/hmda08draft.pdf>.

<sup>2</sup> Rates referenced here are coupon interest rates on 30-year fixed-rate mortgages. FHA insures very few adjustable rate or 15-year term mortgages.

<sup>3</sup> FHA does not collect data on the prior mortgage payment amounts for conventional market borrowers coming into FHA. However, it is likely that those borrowers are saving amounts comparable to FHA streamline refinance borrowers.

<sup>4</sup> Following passage of the Act, FHA issued lender guidelines stopping the acceptance of loans with seller-funded downpayments starting in October 2008. Because of lags between loan origination and insurance endorsement, there were still some cases in the endorsement pipeline in early 2009.

At the same time, FHA's earlier books are experiencing elevated levels of stress in the present economic downturn. The FY 2005 – FY 2008 books-of-business have been especially vulnerable to income and job loss, and are affected by significant home-price declines across the country. The national unemployment rate, which was under 5 percent from 2005 through 2007, has now risen to 9.8 percent, the highest level since 1983.<sup>5</sup> According to the Federal Housing Finance Agency House Price Index, home prices at the national level peaked in mid-2007. Independent forecasts suggest that prices will not finish their decline until sometime in 2010. The story of FHA's financial status at the end of FY 2009 is then the tale of two portfolios. The older portfolio has high rates of delinquencies and is expected to have high rates of insurance claims in the future. The new portfolio, which soon will be larger than the older portfolio, is expected to have more modest claim rates over the life of the loan guarantees. Current delinquency rates by book-of-business are shown in Table 3.

The FY 2007 book, in particular, is showing to-date claim-rate experience that puts it on a par with FHA's worst-ever books from the early 1980s. One should not, however, equate the stress on FHA's portfolio with that of conventional market mortgage portfolios. FHA did not participate in exotic mortgages, nor did it loosen its underwriting to permit less than full documentation loans. FHA also does not permit piggy-back structures that use second mortgages to fund downpayments, nor does it permit prepayment penalties. As noted by the Mortgage Bankers Association in its quarterly National Delinquency Survey, FHA's delinquency and in-foreclosure rates remain far below those of the subprime sector.<sup>6</sup> A recent edition of the Barclays Capital Mortgage Credit Tracker (August 2009) indicated that to-date subprime defaults (foreclosures) have amounted to 14.5 percent of original loan balances for the 2005 book, 21.2 percent for the 2006 book, and 15.5 percent for the 2007 book. Comparable statistics on claims for FHA are just 6.4 percent for 2005, 5.2 percent for 2006, and 2.8 percent for 2007.<sup>7</sup>

Loans insured since January 2009 should provide net positive revenues (after claim payments) for FHA. They do not have seller-funded downpayment loans, they include significant volumes of refinance activity with major monthly-payment reductions, and they have the stronger underwriting qualities mentioned above (higher incomes, higher credit scores, and lower payment burdens). The FY 2009 book is already showing its strength through lower rates of early-payment default. The early-payment default rate—as measured by 90-day delinquencies within the first six monthly payment cycles—peaked for FHA loans with originations in May 2007. It has been declining steadily since May 2008 and, as of January 2009, was just 59% of the 2007 peak. This improvement is the result both of higher underwriting quality, and what is hoped to be the passing of the peak period of employment contraction in the economy. (See Table 4.)

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<sup>5</sup> U.S. Department of Labor, Bureau of Labor Statistics, seasonally adjusted national unemployment rate series. Data as of September 2009.

<sup>6</sup> The worst-performing conventional loans have been the subprime ARMs. According to the Mortgage Bankers Association National Delinquency Survey for 2009Q2, the seriously delinquent rate (90-day delinquencies, plus in-foreclosure and in-bankruptcy) for all subprime loans was over 26 percent. The rate for FHA loans was under eight percent.

<sup>7</sup> The data used by Barclays on subprime portfolio performance comes from Loan Performance. FHA statistics shown here are based on counts rather than loan balances; they are by calendar year of origination to provide comparability with conventional market portfolios, and are as-of September 30, 2009.

## Outline of this Report

This report to Congress is on the financial status of the Mutual Mortgage Insurance (MMI) Fund. That Fund is the umbrella under which FHA operates its single-family insurance programs. The MMI Fund itself is principally comprised of a series of accounts held at the U.S. Treasury. They include business accounts for managing the everyday receipts and expenditures of the insurance operations—which are called Financing Accounts—and an account established to help manage the capital ratio requirement—which is called the Capital Reserve Account.<sup>8</sup> The Capital Reserve Account was established to facilitate the accounting required for managing the capital ratio requirement that exists for the Fund, and that will be discussed in this report. However, FHA’s MMI Fund programs, like all Federal government direct-loan and loan-guarantee programs, operate with the full-faith-and-credit of the U.S. government. They also operate with what is called “permanent and indefinite budget authority,” which provides direct access to the U.S. Treasury for any funds that might be needed to pay extraordinary claim obligations.<sup>9</sup> Thus, FHA programs are never in any jeopardy of lacking sufficient funds to pay insurance claims. That would be true even in the absence of a Capital Reserve Account.

Four primary operational goals for MMI Fund programs are defined in the National Housing Act. They are:<sup>10</sup>

- 1) maintaining an adequate capital ratio;
- 2) meeting the needs of homebuyers with low downpayments and first-time homebuyers by providing access to mortgage credit;
- 3) minimizing the risk to the Fund and to homeowners from homeowner default; and
- 4) avoiding adverse selection.

We now discuss each of these in turn.

## **Maintaining an Adequate Capital Ratio**

The MMI Fund has been required to be self-supporting since its inception in 1934. The capacity to be self-supporting through periods of economic stress was first tested in a significant way in the 1980s. An independent actuarial analysis completed in 1990 indicated that FHA would likely use up most of its MMI Fund reserves to pay for future claims on the 1980s books of business. More importantly, that study found that premium rates were insufficient to pay for expected claims on new insurance commitments going forward.<sup>11</sup> The conclusion was that the MMI Fund was financially solvent at the time, but not sound going forward.

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<sup>8</sup> For pre-1992 books of business there are what are called Liquidating Accounts, which are business accounts like the Financing Accounts. There is very little activity left in the pre-1992 books.

<sup>9</sup> Get USC citation for the Federal Credit Reform Act of 1990.

<sup>10</sup> See 12 USC 1711(h)(2).

<sup>11</sup> *An Actuarial Review of the Federal Housing Administration’s Mutual Mortgage Insurance Fund*. Washington, DC: Price Waterhouse, Office of Government Services, June 6, 1990.

In response to these findings, the Administration and the Congress worked together to pass the Cranston-Gonzales National Affordable Housing Act of 1990 (NAHA).<sup>12</sup> NAHA spelled out a metric and a standard for gauging the financial status of program reserves in a capital-ratio calculation. The centerpiece of the capital-ratio calculation is an estimate of economic net worth. Economic net worth is a net asset position, after booking a liability for loan loss reserves. Those loan loss reserves are to be sufficient for paying all projected future insurance claims, after accounting for expected future premium revenues. Economic net worth is then a measure of unencumbered or excess reserves that would be available to pay for any unforeseen losses on outstanding loan guarantees. The process of estimating economic net worth and the resulting capital ratio assumes a business wind-down scenario where there is no new business available to provide any additional resources. The outstanding portfolio must stand on its own. In NAHA, FHA was required to raise premiums on new books of business in order to restore the financial soundness of MMI programs going forward, to maintain reserves in the face of expected future outlays against existing books of business, and to meet a new capital reserve threshold of two percent. While NAHA gave HUD until 2000 to meet the two percent requirement, FHA met that level in 1995.<sup>13</sup>

Today, as in 1990, recent books-of-business are experiencing elevated levels of stress. That is due both to historic declines in home prices around the country, and to elevated levels of income loss and unemployment. FHA's total reserves are higher than they were in 1990, measuring 4.5 percent of insurance-in-force today versus less than three percent in 1990. Yet, as in 1990, the independent actuarial studies highlighted in this report show that FHA could use-up most of its current reserves paying anticipated future insurance claims, in the absence of any new revenues from future books of business. The calculated net capital ratio for FY 2009 is below the required two-percent level, and is estimated to be just 0.53 percent, which is below where it was in 1990.

The primary difference today is that the just-completed actuarial studies show that FHA's capital reserve ratio will not dip below zero under most of the economic scenarios considered. Under these scenarios, premium rates are sufficient to pay for claims on new books of business, contribute toward the ongoing costs of expected claims on the older books, and then to start rebuilding capital in just a few years. The actuarial studies, as summarized here, indicate that the MMI Fund could regain a two percent net capital ratio as early as FY 2012.<sup>14</sup> In 1990, FHA only charged a periodic premium and not an up-front premium. The periodic (monthly) premium was assessed at an annual rate of 0.50 percent of the loan balance.<sup>15</sup> Today, FHA charges both a periodic premium and an up-front premium. The periodic is still 0.50 percent for loans with original loan-to-value ratios of up to 95 percent, but is now 0.55 percent for all loans with higher

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<sup>12</sup> Public Law 101-508, November 5, 1990. For discussion of policy development leading to passage of this Act see: Weicher, John, "FHA Reform: Balancing Public Purpose and Financial Soundness," *Journal of Real Estate Finance and Economics*, vol. 5 (1992), 133-150.

<sup>13</sup> *An Actuarial Review for Fiscal Year 1995 of the Federal Housing Administration's Mutual Mortgage Insurance Fund, Final Report*. Washington, DC: Price Waterhouse, LLP, June 5, 1996.

<sup>14</sup> See, *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund (Excluding HECMs) for Fiscal Year 2009*. Rockville, MD: Integrated Financial Engineering, Inc, November 6, 2009; *An Actuarial Analysis of FHA Home Equity Conversion Mortgage Loans in the Mutual Mortgage Insurance Fund Fiscal Year 2009*. Fairfax, VA: IBM Global Business Services, October 12, 2009.

<sup>15</sup> Each year, the new annual premium is established as 0.50 percent of the estimated mid-year loan balance and distributed across the year in 12 monthly payments.

ratios.<sup>16</sup> The up-front premium rate today is 1.75 percent for purchase and fully-underwritten refinance loans and 1.50 percent for streamline refinance loans.<sup>17</sup>

## The FY 2009 Actuarial Studies

### *Principal Findings*

FHA has had annual, independent actuarial studies of the MMI Fund since 1991. This year the base contract for this service was augmented by a second contract to perform an actuarial study of the FHA reverse-mortgage insurance program, which is known as the Home Equity Conversion Mortgage (HECM) program. HECM is included as an MMI Fund program for the first time in FY 2009. It is a relatively small program when compared with the standard single-family programs—having an annual insurance volume of \$30 billion—but it provides an important source of liquidity for senior citizens who have significant home equity yet low incomes or else lack liquid assets. Because reverse mortgages are fundamentally different from standard “forward” mortgages, a separate analysis is required for HECM.

The complete reports submitted by the actuarial contractors are available to the public on the [hud.gov](http://hud.gov) internet site.<sup>18</sup> Table 5 of this report provides the fundamental result of those actuarial studies. It shows that FHA’s capital resources have grown from \$27.2 billion at the start of the year, to \$30.7 billion at year’s end.<sup>19</sup> That represents an overall capital-resource ratio against outstanding loan guarantees of 4.5 percent. The increase in capital resources is primarily due to premium revenues collected on new insurance in FY 2009. FHA collects a significant share of total premium revenues at the time of insurance endorsement, and FY 2009 yielded a record volume of new insurance commitments.

At the same time, expected future costs of outstanding loan guarantees have also grown in FY 2009, with the continued weakness in many housing markets across the country. Last year, the estimated amount of earmarked loss reserves necessary to cover expected net losses on future cash flows was \$14.3 billion. This year it has increased to \$27.1 billion. That amount is seen in Table 5 as the Present Value of Cash Flows on Outstanding Insurance. The net result is that the actuarial studies suggest FHA needs to reserve an additional \$12.8 billion for future losses on current business. Once those additional loss reserves are accounted for, then the estimated

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<sup>16</sup> These are the maximum rates allowed per the National Housing Act. The Act also prescribes a maximum 0.25 percent annual premium rate on loans with terms of 15-years or less, and FHA can only charge a periodic/annual premium on these loans if the loan-to-value ratio is 90 percent or greater. NAHA established a schedule that require loans with higher loan-to-value ratios to pay periodic premiums for more years. Today, FHA ends collection of periodic premiums when the loan balance amortizes to 78 percent of the original house value. Because homeowners refinance much more quickly and more often than they did in 1990, extending collection of premiums for longer periods of time would not have a significant impact on the finances of the MMI Fund.

<sup>17</sup> Today the maximum permissible up-front premium, per the National Housing Act, is 3.0 percent.

<sup>18</sup> They are located in the Office of Housing Reading Room page, under Reports and Data, and can be found at <http://www.hud.gov/offices/hsg/hsgroom.cfm>.

<sup>19</sup> FHA’s annual, audited financial statements now show year-end capital resources of \$31.8 billion for FY 2009. That figure was not available to the actuarial contractors at the time their analysis was performed.

economic net capital position of the MMI Fund falls to \$3.6 billion. When measured against outstanding insurance-in-force of \$685 billion, this yields a net capital ratio of 0.53 percent.<sup>20</sup>

The Present Value of Future Cash Flows on Outstanding Insurance comes from estimates of how loans will prepay or claim in the future, and the recoveries on those claims. These loan-performance estimates are functions of econometric models of past borrower behavior, extrapolated to predict future behavior using forecasts of economic conditions. The economic expectations built into these estimates are from a third-party macroeconomic forecasting firm, IHS Global Insight, and they suggest that house prices may yet fall another six to seven percent in FY 2010.<sup>21</sup> The macroeconomic forecasts also suggest that the current, low mortgage interest rates will continue through FY 2010, and will only slowly increase after that.

Both home-price declines and continued low interest rates have negative effects on the value of outstanding books of business. Home price declines increase the probability of foreclosures when households have financial disruptions, and low interest rates result in refinancing actions that reduce future revenues for outstanding books. FY 2009 saw significant refinance activity out of recent-vintage books, especially starting in January 2009. Borrowers who took out loans in FY 2008 and refinanced in FY 2009 saved, on average, \$135 per month. This improves their abilities to remain current on monthly loan payments, and thus reduces the risk of default for FHA. Those who refinanced their FY 2007 loans saved an average of \$123 per month, and those refinancing FY 2006 loans saved \$115 per month, on average. (See Table 6.) These refinance actions provide valuable loans for FY 2009, but they also have the effect of eroding the value of earlier books.<sup>22</sup>

### *The Out-years*

Estimates of economic net worth and the capital ratio are as of a point in time. The actuarial studies compute estimates for end-of-year positions covering the period FY 2009 – FY 2016. Estimates for future years include the addition of projected new business for each of those years.<sup>23</sup> Such out-year projections are important for understanding what will likely happen to the MMI Fund's capital resource position over time. The outstanding business at the end of FY 2009 is expected to drain a significant portion of current capital resources over the next five years. The

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<sup>20</sup> Previous Actuarial Reviews reported capital ratios calculated on both unamortized and amortized insurance-in-force. Those Reviews then focused only on the unamortized calculation. This was due to wording in the National Housing Act that mislabeled the definition of amortized as unamortized (see 12 USC 1711(f)(4)(D)). Indeed, the National Housing Act does define the denominator of the capital ratio calculation as outstanding loan balances (amortized balances, as commonly understood). This distinction has very little significance in the calculation of the capital ratio this year, but it could have significance in future years. This is because current low interest rates suggest that the FY 2009-2011 books will have low and slow prepayment speeds. Over time, there will then be large differences between unamortized (original loan balances) and amortized (current loan balances) insurance-in-force.

<sup>21</sup> The econometric models use, and thus the economic forecasts are for the Federal Housing Finance Agency national House Price Index. The econometric models first mark-to-market the entire FHA portfolio at the start of the forecast period, using metropolitan and state non-metro price series, and then use a national price forecast in the future. Locality and property variations around that national average price forecast are accounted for with a price-diffusion process.

<sup>22</sup> As also seen in Table 6, there was significant refinance activity just within the FY 2009 book. Borrowers who took out loans in the summer and fall of 2008, when interest rates were around 6.5 percent, refinanced in the following spring and summer with savings of \$150 per month, on average. This serves to make the FY 2009 book even stronger.

<sup>23</sup> Each new book of business is then given projections of loan performance and resulting cash flows for the life of the loan guarantees, which is typically 30 years.

question then is to what extent new business might be expected to replace those funds and thus maintain a higher level of MMI Fund capital resources than what would be indicated solely by winding down the current portfolio.

Figure 1 shows the out-year projections of capital resources from the actuarial studies. That Figure includes not only the base-case projections, but also projections under several alternative economic scenarios. Those alternatives are designed to test the sensitivity of outcomes to various changes in the economic forecast, and are discussed below. The base-case results in Figure 1 show that the MMI Fund is expected to experience net cash outflows for the next two years. After that, with an economic recovery in full swing, capital resources are expected to begin to rise. Capital resources over the next two years are expected to decline to \$22.1 billion, as premium revenues from current and newly added books are predicted to be less than net claim expenses during that period. At the same time, outstanding (amortized) insurance-in-force is expected to rise to \$1,023 billion, yielding a capital-resource ratio of 2.16 percent at the low point predicted for the end of FY 2011.

### Risks Facing the Fund

Estimates of capital resources, economic net worth, and the resulting net capital ratio are based on assumptions concerning future economic conditions and homeowner responses to those conditions. Having \$3.6 billion in excess reserves today provides a thin margin for a \$685 billion portfolio. However, it should be remembered that this is after reserving for expected net outlays over a 30-year period. The actuarial projections are for net outlays in FY 2010, on the current, outstanding portfolio, of \$11.4 billion, after accounting for claim payments, recoveries, and premium revenues. If loss reserves were booked for net expected loss-on-claims in the next year, as is required for most private firms, then FHA would book loan loss reserves of \$13.5 billion, and the MMI fund capital ratio would be 2.0 percent.<sup>24</sup>

The independent actuaries ran a number of sensitivity analyses to show what the capital ratio would be under different economic scenarios. A summary of those analyses is provided in Table 7. The actual capital resources available to FHA under each scenario are shown in Figure 1. Three scenarios shown in Table 7 result in capital ratio estimates below the base case. They are the Deeper Housing Recession, Higher Loss Severity Rates, and Downward Interest Rate Shock.

The Deeper Housing Recession scenario has home prices falling more than 13 percent from mid-2009 to mid-2010, for a peak-to-trough cyclical decline of 19 percent.<sup>25</sup> This contrasts with the base-case forecast of a decline of between 8 and 9 percent during that 4-quarter time period, and a peak-to-trough decline of 14 percent. When the greater stress is applied to the FHA portfolio the economic net worth of the Fund becomes negative. That implies that FHA would require net

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<sup>24</sup> Private firms reserve for losses expected over the next 12 months, as required by Financial Accounting Standards 5 and 114. FHA loss-reserve accounting is based on expected cash outflows and inflows for the entire life of the underlying loan guarantees, as required by OMB Circular A-11, which spells out budget accounting requirements under the Federal Credit Reform Act of 1990.

<sup>25</sup> The FHFA house price index does not fluctuate as widely as does the better-known Case-Shiller index. The FHFA index is more broadly based, and it does not include homes purchased or refinanced with non-agency-backed loans. The 19 percent house price decline in the Deeper Housing Recession scenario is roughly equal to a 27 percent decline in the 10-city Case-Shiller index.

receipts from new insurance written in the coming years to assist in paying for expected losses on outstanding books. That this is an extremely stressful scenario is seen in that expected claim and loss rates in the base-case scenario start at very high levels. The base-case scenario creates an expectation that single-family (forward) loans from the FY 2006 – FY 2008 books will, as they continue to season, have final, lifetime claim rates of 20 percent or more. That is on a level that matches the worst experience of the 1980s. To-date, only the FY 2007 book has actual (early-years) experience that is as high as those of early 1980s books. Thus, the Deeper Housing Recession scenario creates a situation that is much worse than was the 1980s.

The Higher Loss-Severity Rate Scenario looks at what would happen were there to be a permanent change in foreclosed property sale processes, so that recovery rates on those sales (percent of defaulted loan balance) falls by five percentage points, and stays there throughout the future forecast period. Under such a scenario, the economic net worth of the MMI Fund falls to nearly zero in the present time, and it recovers more slowly than it does in the Deeper Housing Recession scenario.

The Downward Interest Rate Shock scenario produces an even larger negative Economic Net Worth for the MMI Fund than does the Deeper Housing Recession. It envisions a protracted economic recession where short-term interest rates go to zero and home mortgage interest rates fall to around two percent. Interest rates are held in that position for three years. This situation results in such high rates of run-off from existing books that there is scarcely any premium revenues left to pay for insurance claims. Of course in the current environment, where private capital for mortgage guarantees is scarce, that business would likely come back to FHA in the form of streamline refinance activity in future books-of-business, but that return business is not included in this scenario.<sup>26</sup> Thus, in this scenario, FHA would lose so much premium revenue that the MMI Fund would run out of capital resources in FY 2011, requiring \$1.6 billion in borrowing from the Treasury in FY 2012 to pay its net claim expenses..<sup>27</sup>

High prepayment speeds, when accompanied by high levels of new (refinance) insurance endorsements, cause the value of outstanding books to deteriorate, but the value of new books increase as a result. This points to limitations of the net capital ratio as the primary measure of financial status and soundness. Table 7 shows the actuarial projections of the capital ratio for each future year, through FY 2016, as the economic recession runs its course, and as new books of business are added to the portfolio. Each sensitivity analysis also includes estimates of future capital ratios. In the base case, the capital ratio for the MMI Fund is expected to return to two percent by the end of FY 2012, without any risk management or underwriting changes on the part of FHA. It is simply a function of the recession running its course and, as a result, new books of business generating significant amounts of net revenues. The bottom-line is that the FHA MMI Fund portfolio has good prospects for the future.<sup>28</sup>

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<sup>26</sup> The actuarial analysis does not employ a high rate of recapture by FHA, but rather uses an historical recapture rate of 19 percent.

<sup>27</sup> Budget accounting rules would actually require FHA to secure the funds in advance, as soon as negative economic value were recognized, as opposed to waiting until the cash is actually required.

<sup>28</sup> These estimates of future capital ratios also assume that the underwriting quality of the FHA single-family (forward loan) books returns to what it was before the recent tightening by the conventional market by FY2013. That is, it assumes a full recovery by the private mortgage insurance industry, and some form of future guarantee

FHA does not rely upon annual calculations of the capital ratio for purposes of monitoring and managing the health of the MMI Fund. Senior management receives internal reports on a monthly basis that provide a more robust set of analytical metrics. Those measures include delinquency rates by various subportfolio break-outs (including book of business), foreclosure and claim trends, operating revenues and expenses, underwriting characteristics, product volumes and shares, performance of loss mitigation efforts, and other factors. FHA also does an annual review of the entire insured portfolio with the Office of Management and Budget, as part of the budget re-estimation process.

### Expectations for Portfolio Experience in FY 2010

The actuarial projections for MMI Fund single-family programs discussed above suggest that continued declines in home prices into FY 2010 will result in a measurable increase in claim payments. This is confirmed by recent trends in foreclosure starts. As seen in Table 8, the number of new foreclosure starts has increased significantly over the past year. They suggest that actual foreclosure completions on FHA-insured loans in FY2010 should be greater than 100,000. Indeed, the actuarial projections are for 116,000 foreclosure claims in FY 2010. That compares with 70,000 foreclosure claims in FY 2009 and 56,400 in FY 2008.<sup>29</sup>

### Current Actions Taken to Strengthen the MMI Fund

FHA recently announced a series of policy changes designed to reduce risk on both single-family forward and HECM reverse mortgages. Those changes are not reflected in the independent actuarial studies or the consolidated results shown in this report. For HECM, FHA enacted across-the-board reductions of 10 percent to the allowable principal limits (ML 2009-34).<sup>30</sup> The principal limits define the maximum amount of take-out per each dollar of house value. HECM loans grow over time as both interest and mortgage insurance premiums accrue and are added to the loan balance. The principal limits are determined both by the borrower's age and current interest rates. Lower take-outs yield lower loan balances over time, and thus reduce the chance that FHA will have a loss when borrowers move out of their homes and the properties are sold.<sup>31</sup>

With single-family mortgages, FHA has implemented new procedures to expand its partial-claim loss-mitigation program to assist borrowers in cases where there is reduced income (ML 2009-23), tightened eligibility requirements for approved mortgagees (ML-2009-31), shortened the

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program that matches the former role of Fannie Mae and Freddie Mac, by 2013. Recovery in the conventional market implies lower underwriting quality for new FHA business.

<sup>29</sup> The 70,000 for FY 2009 is a preliminary estimate. Due to delays in filing and processing claims, the final number is not yet known. Total claims reported by FHA will be higher, due to the include of preforeclosure (short) sales in those counts. The total-claim projection for FY 2010 is 125,000.

<sup>30</sup> Mortgagee Letter 2009-34, Home Equity Conversion Mortgage (HECM) – Principal Limit Factors, September 23, 2009.

<sup>31</sup> HECM loans are due-and-payable when the borrower no longer resides in the home. There are no monthly payments. FHA provides a refinance option for HECM, which can permit a higher dollar take-out if home prices have grown since the first HECM was originated.

appraisal validity period (ML 2009-30), increased safeguards for appraisal independence (ML 2009-28), and established risk-controls on streamline refinance transactions (ML 2009-32).<sup>32</sup>

HUD has also hired its first ever Chief Risk Officer for FHA, who will be responsible for comprehensive monitoring and oversight of financial risk, operations risk, and counterparty risk.

## **Meeting the Needs of Homebuyers**

Table 9 shows how FHA continues to support homebuyers who have limited resources. Nearly 86 percent of homebuyers relying upon FHA mortgage insurance in FY 2009 had downpayments of less than five percent. It is also the case that 79 percent of FHA's purchase-loan borrowers were first-time homebuyers. Table 10 indicates the extent to which FHA is meeting the needs of homebuyers today. In the second quarter of 2009, FHA facilitated home buying for one half of all first-time buyers in the entire national housing market.

## **Minimizing the Risks from Default**

FHA has maintained an aggressive program of default intervention since receiving statutory authority for loss mitigation programs in 1996. Lenders servicing FHA loans are required to reach out to delinquent borrowers and work with them to see if assistance is needed, and if it could help overcome short-term financial difficulties. FHA pays servicers for actions related to completing long-term repayment plans, loan modifications, and actions taken to bring loans current (via FHA funds) when borrowers can resume payments but cannot pay back arrears from current income ("partial claims").

This intervention program comes under the heading of loss mitigation activities for FHA. As the number of delinquencies have increased, so too have servicer interventions to help cure them. Table 11 shows the rapid increase in this activity since the beginning of 2007. The number of interventions in 2009 is more than double the number seen in early 2007, keeping pace with the growth of 90-day delinquencies in the FHA-insured portfolio. In the face of rising unemployment in the economy, the number of home-retention interventions has also nearly doubled in the same time period. Home retention interventions throughout this period have consistently been about 95 percent of all loan servicer actions, with the remainder being preforeclosure sales and voluntary deed transfers. While sound underwriting criteria and lender approval processes provide front-end risk barriers for meeting that National Housing Act operational goal of minimizing risk to the Fund and to homeowners from default, FHA's loss mitigation programs provide an important back-end risk barrier.

Ninety-day delinquencies that began in early 2007 have had a transition-to-foreclosure rate of about 20 percent.<sup>33</sup> The growth and strength of FHA's loss mitigation intervention program is

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<sup>32</sup> Mortgagee Letter 2009-23, Making Home Affordable Program FHA's Home Affordable Loss Mitigation Option, July 30, 2009; ML 2009-28, Appraiser Independence, September 18, 2009; ML 2009-30, Appraisal Validity Periods, September 18, 2009; ML 2009-31, Strengthening Counterparty Risk Management, September 18, 2009; and ML 2009-32, Revised Streamline Refinance Transactions, September 18, 2009.

expected to keep that failure rate in the same range going forward. Indeed, it is possible for the rate of transition from 90-day delinquency to foreclosure to actually decline in the future, with the advent of FHA's expanded partial claim program, under the umbrella of the Administration's Home Affordable Modification Program (HAMP) initiative.<sup>34</sup> Using new authorities provided by the Helping Families Save Their Homes Act of 2009, FHA can now assist borrowers who are delinquent due to a permanent reduction in income, yet who have a continued commitment to the property. FHA will use its partial claim authority to both pay for current arrears, and to buy down the principal balance of the loan. That second, and new option, is what can permit a loan servicer to reduce the borrower's monthly payments to an affordable level, when FHA's guidelines are fully met. FHA estimates that between 15 and 30 percent of borrowers now destined to foreclosure could otherwise be helped through the HAMP initiative.

### **Avoiding Adverse Selection**

Adverse selection is a phenomenon whereby an insurer's product is mispriced in such a way as to only, or primarily attract above-average risks. If premiums are based on average risk, then the result of adverse selection is a portfolio destined to result in net losses. Adverse selection is a particular problem during periods when there are significant numbers of inexpensive and easily accessible conventional market alternatives to FHA insurance. There was concern that FHA was being "adversely selected" during the recent housing boom, when low- and no-downpayment options were prevalent in the conventional market. FHA's endorsement and market-share decline during that period was directly traceable first to increased subprime activity and, second, to expanded affordable housing initiatives at Fannie Mae and Freddie Mac.

FHA was also adversely selected from 2000 through 2008 because it was the only guarantor willing to accept loans using seller-funded downpayments. Such downpayments were channeled through nonprofit organizations in order to meet FHA requirements on direct sources of funds.<sup>35</sup> Those facilities created too many homeowners in the FHA portfolio that were not equipped for the financial responsibilities of home ownership. Indeed, the FY 2009 MMI Fund actuarial study for single-family loans notes that, if FHA had not insured any loans with seller-funded downpayment assistance, the net capital ratio today would still be above the statutory required two percent. FHA's estimated economic net worth would be \$10.4 billion higher today were it not for those loans.<sup>36</sup> Table 12 details the experience of these loans relative to other home purchase loans insured by FHA from FY 2000 through FY 2008. Their claim rates have consistently been between 2.5 and three times those of other FHA-insured home purchase loans.

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<sup>33</sup> More recent defaults have had lower rates of foreclosures, to date, but are expected to reach the 20 percent level over time.

<sup>34</sup> See Mortgagee Letter 2009-23, *Making Home Affordable Program: FHA's Home Affordable Modification Loss Mitigation Option*, July 30, 2009.

<sup>35</sup> FHA permits downpayment assistance from relatives, employers, government agencies, and IRS registered, tax-exempt charitable nonprofit organizations. The IRS ruled in 2006 (Revenue Ruling 2006-27) that organizations whose primary mission was to channel funds from property sellers to property buyers did not qualify for tax-exempt status.

<sup>36</sup> Integrated Financial Engineering, Inc., *op.cit.*, page 52.

In the current environment, where private, conventional market capital is not readily available for low-downpayment lending, there are no signs that FHA might be experiencing adverse selection. However, risk of that phenomenon will increase as the economy improves and the conventional mortgage market recovers and relaxes its currently stringent underwriting standards. Today FHA has a very favorable combination of high credit scores and income levels in new insurance endorsements. As such favorable conditions end, FHA will monitor the underwriting quality of new loans and make premium and underwriting changes, as necessary, to minimize any potential for problems of adverse selection in the future.

Fiscal Year	Home Purchase Loans	Conventional-to-FHA Refinance	FHA-to-FHA Refinance	HECM	All Single-Family Loans
2000	\$ 86.892	\$ 3.347	\$ 3.976	\$ 0.841	\$ 95.056
2001	87.729	5.202	24.764	1.119	118.814
2002	99.647	7.790	40.661	1.978	150.075
2003	79.898	7.984	71.353	3.012	162.247
2004	72.719	7.351	35.906	6.903	122.880
2005	43.556	4.480	14.322	8.886	71.244
2006	39.997	8.853	6.452	17.982	73.283
2007	37.518	16.612	5.706	24.625	84.462
2008	101.991	63.583	15.593	24.244	205.412
2009	171.735	87.019	71.729	29.053	359.537

Source: US Department of HUD/FHA; October 2009.

Table 2a. FHA Single Family Insurance Portfolio Risk Characteristics – Average Underwriting Values <sup>a</sup>			
Fiscal Year <sup>b</sup>	Credit Score <sup>c</sup>	Mortgage Payment Ratio <sup>d</sup>	Total Debt Payments Ratio <sup>e</sup>
2005	639	25.19%	38.29%
2006	641	25.77	39.11
2007	630	26.11	39.27
2008	647	26.63	40.33
2009	681	24.24	36.85

<sup>a</sup>These characteristics are for fully-underwritten loans only and do not include streamline refinance loans.

<sup>b</sup>Based on date of insurance endorsement.

<sup>c</sup>Based on the composite decision credit score used for underwriting purposes.

<sup>d</sup>Monthly mortgage payment to monthly income.

<sup>e</sup>Monthly fixed obligations to monthly income.

Source: US Department of HUD/FHA; October 2009.

Table 2b. FHA Single Family Insurance Portfolio Risk Characteristics – Percentage of Dollar Volumes of Insurance Endorsements in Various Risk Classes <sup>a</sup>			
Fiscal Year <sup>b</sup>	Percent of Dollars Insured by Risk Metric		
	Credit Score below 620 <sup>c</sup>	Credit Score of 720 or Better <sup>c</sup>	Income above Area Median <sup>d</sup>
2005	40.57%	12.55%	33.56%
2006	39.36	13.44	39.37
2007	46.90	10.37	47.75
2008	33.56	16.27	55.48
2009	12.88	29.52	53.74

<sup>a</sup>These characteristics are for fully-underwritten loans only and do not include streamline refinance loans.

<sup>b</sup>Based on date of insurance endorsement.

<sup>c</sup>Based on the composite decision credit score used for underwriting purposes.

<sup>d</sup>Based on HUD estimated county-level median incomes used for determining fair market rents. Monthly mortgage payment to monthly income.

Source: US Department of HUD/FHA; October 2009.

**Table 3. FHA-Single-Family Insurance  
Delinquency Rates by Insurance Cohort Year  
September 2009**

Year of Insurance	Insurance Shares <sup>a</sup>	Delinquency Categories and Rates						
		In Delinquency <sup>b</sup>	30 Day	60 Day	90+ Day	In Foreclosure	In Bankruptcy	Seriously Delinquent <sup>c</sup>
2004	7.7%	21.47%	7.18%	3.13%	6.56%	2.82%	1.77%	11.14%
2005	5.7	24.51	7.81	3.61	7.61	3.44	2.01	13.05
2006	5.4	26.90	7.83	3.81	8.88	4.27	2.04	15.20
2007	5.7	32.27	9.15	4.54	11.37	5.22	1.94	18.53
2008	15.7	23.98	7.95	3.87	8.34	2.85	0.94	12.13
2009	31.4	6.46	3.70	1.15	1.26	0.23	0.11	1.60
All Loans	100.0%	17.71%	6.42%	2.74%	5.33%	2.06%	1.13%	8.52%

<sup>a</sup>Based on numbers of Loans.

<sup>b</sup>Includes all loans 30 or more days past due, including those in bankruptcy or foreclosure.

<sup>c</sup>Includes all loans 90-days past due plus all in-bankruptcy and in-foreclosure cases.

Source: US Dept of HUD/FHA; October 2009.

Table 4. FHA Single-Family Insurance  
Early Payment Default Rates<sup>a</sup>  
By Month of Loan Origination

Year	Month	Rate
2007	Jan	2.06%
	Feb	2.15
	Mar	2.40
	Apr	2.47
	May	2.60
	Jun	2.65
	Jul	2.60
	Aug	2.46
	Sep	2.21
	Oct	2.17
	Nov	2.31
	Dec	2.31
2008	Jan	2.24
	Feb	2.15
	Mar	2.22
	Apr	2.21
	May	2.09
	Jun	2.15
	Jul	2.09
	Aug	1.75
	Sep	1.63
	Oct	1.51
	Nov	1.44
	Dec	1.49
2009	Jan	1.42

<sup>a</sup>90-day defaults in first 6 payment months.

Source: US Department of HUD/FHA; October 2009.

<b>Table 5. MMI Fund Economic Value and Capital Ratio Calculations for FY 2009</b> (all dollars are in millions)				
	Fy 2008 MMI Fund <sup>a</sup>	FY 2009 Activity and End-of-Year Positions		
		Single Family	HECM <sup>b</sup>	MMI Fund
<b>Beginning-of-Year Positions<sup>c</sup></b>				
Cash	\$ 9,210			
Investments	19,244			
Properties and Mortgages	2,261			
Other Assets and Receivables	<u>127</u>			
Total Assets	\$ 30,842			
Liabilities (Accounts Payables)	<u>3,639</u>			
Net Capital Resources	\$ 27,203	\$ 27,203		\$ 27,203
<b>Actuarial Calculations<sup>d</sup></b>				
Net Gain from Investments		\$ 386	\$ 0	\$ 386
Net Insurance Income		2,516	614	3,130
Expected Recoveries on Assigned HECM Mortgages <sup>e</sup>		<u>0</u>	<u>0</u>	<u>0</u>
<b>Capital Resources at End-of-Year</b>		<b>\$30,105</b>	<b>\$ 614</b>	<b>\$30,719</b>
Present Value of Future Cash Flows on Outstanding Insurance		<u>(27,373)</u>	<u>295</u>	<u>(27,078)</u>
<b>Economic Net Worth</b>	<b>\$ 12,908</b>	<b>\$ 2,732</b>	<b>\$ 909</b>	<b>\$ 3,641</b>
End-of-Year Unamortized Insurance-In-Force <sup>f</sup>	\$ 429,634	\$686,263	\$28,696	\$714,959
<b>Capital Ratio Using Unamortized Insurance-in-Force</b>	<b>3.00%</b>	<b>0.40%</b>	<b>3.17%</b>	<b>0.51%</b>
End-of-year Amortized Insurance-in-Force <sup>g</sup>	\$ 401,461	\$656,012	\$28,696	\$684,708
<b>Capital Ratio Using Amortized Insurance-in-Force<sup>h</sup></b>	<b>3.22%</b>	<b>0.42%</b>	<b>3.17%</b>	<b>0.53 %</b>

<sup>a</sup>Data in this column are from the FY 2008 Actuarial Review of the MMI Fund.

<sup>b</sup>HECM loans are only included in the MMI Fund starting with FY 2009 insurance endorsements.

<sup>c</sup>Beginning of Year positions are from FHA's audited FY 2008 financial statements.

<sup>d</sup>Actuarial Calculations for Single Family and HECM come from the respective FY 2009 Actuarial Reviews.

<sup>e</sup>There are at present no assigned mortgages from HECMs in the MMI Fund (FY 2009 endorsements).

<sup>f</sup>Unamortized Insurance-in-Force represents original loan balances for forward loans and maximum claim amounts for HECM.

<sup>g</sup>Amortized Insurance-in-Force represents outstanding loan balances for forward loans and maximum claim amounts for HECM.

<sup>h</sup>The National Housing Act defines the capital ratio calculation as being the ratio of economic value to outstanding loan balances. This corresponds to the commonly understood notion of amortized insurance-in-force.

Table 6. FHA Single Family Insurance Streamline Refinance Loans Insured in FY2009 By Source Cohort and Average Borrower Benefits <sup>a</sup>				
Source Cohort	Number of Loans	Source Cohort Share of Total	Monthly Payment Saving <sup>b</sup>	Interest Rate Saving <sup>c</sup>
<b>All</b>	<b>329,439</b>	<b>100.00%</b>	<b>\$ 131</b>	<b>1.22%</b>
2009	81,898	24.86	149	1.21
2008	165,875	50.35	134	1.18
2007	36,587	11.11	123	1.32
2006	19,133	5.81	115	1.31
2005	5,787	1.76	67	0.89
2004	6,344	1.93	70	1.02
2003	5,186	1.57	66	1.10
2002	3,273	0.99	87	1.74
2001	1,721	0.52	99	2.13
2000	838	0.25	101	2.58
Pre-2000	2,797	0.85	82	2.30

<sup>a</sup>Source cohort represents the fiscal year of insurance endorsement on the prior mortgage loan.

<sup>b</sup>Difference between monthly principal and interest payment on prior loan and that on the new refinanced loan. For Adjustable rate mortgages, the difference is based on initial payments in the first year. FHA has not insured many adjustable rate mortgages since the late 1990s.

<sup>c</sup>Difference between coupon rate on previous loan and coupon rate on refinanced loan.

Source: US Department of HUD/FHA; October 2009

<b>Table 7. Projected MMI Fund Capital Ratios through FY 2016 by Economic Scenario<sup>a</sup></b>						
<b>Fiscal Year<sup>b</sup></b>	<b>Base Case<sup>c</sup></b>	<b>Deeper Housing Recession<sup>d</sup></b>	<b>Early Onset of Recovery<sup>e</sup></b>	<b>Upward Interest Rate Shock<sup>f</sup></b>	<b>Downward Interest Rate Shock<sup>g</sup></b>	<b>Higher Loss Severity Rates<sup>h</sup></b>
<b>2009</b>	0.53%	-0.46%	1.79%	1.62%	-2.33%	-0.16%
2010	1.10	0.18	2.38	1.18	-1.03	0.44
2011	1.74	0.91	2.91	1.14	0.02	1.08
2012	2.27	1.52	3.30	1.25	0.96	1.62
2013	2.68	1.98	3.57	1.82	1.50	2.01
2014	2.95	2.30	3.73	2.26	1.88	2.27
2015	3.26	2.64	3.94	2.70	2.26	2.56
2016	3.57	2.99	4.16	3.12	2.63	2.86

<sup>a</sup>Ratios computed here include data on both forward and reverse (HECM) mortgages.

<sup>b</sup>Calculations are as-of the end of each fiscal year. Years after FY 2009 include new insurance written each year in the calculations.

<sup>c</sup>Using the August 2009 economic forecasts of IHS Global Insight.

<sup>d</sup>Uses the July 2009 house price forecast of IHS Global Insight for the first four quarters of the forecast period (FY2010).

<sup>e</sup>Uses the July 2008 house price forecast of IHS Global Insight starting in October 2009, showing no further house price declines.

<sup>f</sup>Increase mortgage interest rates by 300 basis points for FY 2010 – FY 2012.

<sup>g</sup>Decrease mortgage interest rates by 300 basis points for FY 2010 – FY 2012.

<sup>h</sup>Recoveries on foreclosed property dispositions are reduced by 5 percentage points for the entire 30-year forecast period.

Source: FY 2009 independent actuarial reviews of the MMI Fund; Merged report by the U.S. Department of HUD/FHA.

**Table 8. FHA Single-Family Insurance  
Monthly Foreclosure Statistics and Trends**

Year	Month	Insurance in Force	Foreclosure Starts <sup>a</sup>	In Foreclosure <sup>b</sup>	Foreclosure Claims <sup>c</sup>	Foreclosure Starts: 6-month MA <sup>d</sup>	Annualized foreclosure rate <sup>e</sup>
2008	January	3,778,943	6,803	54,220	4,966	5,324	1.57
	February	3,800,639	4,244	53,554	4,910	5,237	1.54
	March	3,837,360	4,919	53,420	5,053	5,367	1.57
	April	3,888,952	5,811	54,481	4,750	5,522	1.46
	May	3,956,600	4,254	54,110	4,625	5,239	1.39
	June	4,043,850	4,460	53,868	4,702	5,082	1.39
	July	4,146,040	6,480	55,691	4,657	5,028	1.34
	August	4,554,269	7,046	57,973	4,764	5,495	1.25
	September	4,366,032	7,447	60,594	4,826	5,916	1.32
	October	4,499,276	7,210	63,012	4,792	6,150	1.27
	November	4,594,000	6,359	64,720	4,651	6,500	1.21
	December	4,687,539	9,380	68,497	5,603	7,320	1.42
2009	January	4,769,802	8,826	72,253	5,070	7,712	1.27
	February	4,833,033	10,223	77,342	5,134	8,240	1.27
	March	4,909,018	11,192	82,536	5,998	8,864	1.46
	April	4,954,215	12,885	89,695	5,726	9,809	1.38
	May	5,053,263	5,845	89,731	5,809	9,723	1.37
	June	5,167,464	5,705	88,655	6,781	9,110	1.56
	July	5,287,971	18,573	100,198	7,030	10,725	1.58
	August	5,411,524	14,602	108,023	6,777	11,272	1.49

<sup>a</sup>Foreclosure starts are imputed by adding Foreclosure Claims to the monthly change in number of loans in-foreclosure.

<sup>b</sup>Numbers of loans in some stage of foreclosure processing at the end of each month.

<sup>c</sup>Number of conveyance claims paid by HUD. These are nearly all for completed foreclosure events.

<sup>d</sup>The six-month moving average (MA) of foreclosure starts is presented here to smooth out variations in actual starts each month.

<sup>e</sup>An annualized foreclosure rate takes the monthly foreclosure claim rate and transforms that into its annual equivalency. That is, if the same foreclosure claim rate continued for 12 straight months, then this shows the final annual foreclosure rate result as a percentage of beginning insurance-in-force.

Source: US Department of HUD/FHA; October 2009.

<b>Table 9. FHA Single Family Insurance Loan-to-Value Rate Distributions for Endorsements in January – August 2009</b>			
LTV Category <sup>b</sup>	Loan Purpose <sup>a</sup>		
	Home Purchase	Refinance	Combined
Up to 80	2.0%	13.3%	6.0%
81-90	5.0	30.7	14.0
91-95	7.2	36.9	17.6
96	55.0	6.0	37.8
96.5	30.7	13.0	24.5

<sup>a</sup>This analysis includes only fully-underwritten loans and not streamline refinancing.

<sup>b</sup>The 96 group represents all loans with LTV ratios above 95% but below the maximum allowable value of 96.5%. The 96.5 group represents all loans at the maximum allowable LTV.

Source: US Department of HUD/FHA; September 2009.

<b>Table 10. First-time Homebuyer Activity and FHA Shares by Calendar Year</b>							
<b>FHA Insurance of Home Purchase Loans</b>					<b>U.S. Home Purchase Activity</b>		
Calendar Year	Home Purchase Loans Insured by FHA (000s)	First-time Homebuyer Share of FHA Purchase Loans	First-time Homebuyer Activity in the Housing Market (000s)	FHA Share of All First-Time Homebuyers	First-time Homebuyer Share	All Purchases (000s)	First-time Homebuyer Loans (000s)
2006	157	79.1	124	4.6	36.0	7,529	2,710
2007	139	79.4	110	4.4	39.0	6,428	2,507
2008	344	77.3	266	12.0	41.0	5,398	2,213
2009	461	78.3	361	38.6	37.9	2,463	935
Qtr 1	182	78.3	143	29.1	50.0	978	489
Qtr 2	279	78.3	218	49.0	30.0	1,485	446

Sources: US Department of HUD/FHA, National Association of Realtors, and National Association of Home Builders; analysis by HUD/FHA. August 26, 2009

Table 11. FHA Single-Family Insurance Foreclosure Avoidance Interventions on 90-day delinquencies, 2007 – 2009<sup>a</sup>

Assistance Quarter	Forbearance <sup>b</sup>	Repayment Plan Activated <sup>c</sup>	Loan Modification <sup>d</sup>	Partial Claim <sup>e</sup>	Preforeclosure Sale <sup>f</sup>	Voluntary Deed Transfer	All Interventions	Home retention interventions
<i>Numbers of Interventions</i>								
2007Q1	2,177	12,757	6,677	2,202	1,181	170	25,164	23,813
2007Q2	2,514	10,970	8,922	2,162	1,208	108	25,884	24,568
2007Q3	2,935	15,050	9,748	2,479	1,095	150	31,457	30,212
2007Q4	3,197	14,466	10,299	2,226	1,071	155	31,414	30,188
2008Q1	5,164	15,856	13,087	3,205	1,021	199	38,532	37,312
2008Q2	5,095	12,481	15,345	3,930	1,524	192	38,567	36,851
2008Q3	6,488	12,905	13,368	4,724	1,541	350	39,376	37,485
2008Q4	10,748	16,050	15,502	6,070	1,925	258	50,553	48,370
2009Q1	8,622	17,400	21,835	6,846	1,878	303	56,884	54,703
2009Q2	10,135	15,927	23,179	4,690	2,535	266	56,732	53,931
<i>Percentage Shares of each Intervention Type</i>								
2007Q1	8.65%	50.7%	26.53%	8.75%	4.69%	0.68%	100%	94.63%
2007Q2	9.71	42.38	34.47	8.35	4.67	0.42	100	94.91
2007Q3	9.33	47.84	30.99	7.88	3.48	0.48	100	96.04
2007Q4	10.18	46.05	32.78	7.09	3.41	0.49	100	96.10
2008Q1	13.40	41.15	33.96	8.32	2.65	0.52	100	96.83
2008Q2	13.21	32.36	39.79	10.19	3.95	0.50	100	95.55
2008Q3	16.48	32.77	33.95	12.00	3.91	0.89	100	95.20
2008Q4	21.26	31.75	30.66	12.01	3.81	0.51	100	95.68
2009Q1	15.16	30.59	38.39	12.04	3.30	0.53	100	96.18
2009Q2	17.86	28.07	40.86	8.27	4.47	0.47	100	95.06

<sup>a</sup>Interventions to avoid unnecessary foreclosures are the responsibility of FHA-approved loan servicers. They operate under guidelines established by FHA. This table summarizes the last recorded intervention activity on each reported delinquency.

<sup>b</sup>Forbearance plans are most often the first step in the process of assisting borrowers to cure delinquencies. These often lead to other options as long-term solutions. The large number of forbearance interventions in 2009Q3 represents borrowers who are actively working with loan servicers toward a resolution plan.

<sup>c</sup>Not all repayment plans listed here are still active. Many have already been completed and the delinquencies cured and some have failed and foreclosure proceedings started.

<sup>d</sup> Loan modifications generally entail adding arrears to the loan balance and resetting monthly payments.

<sup>e</sup> The FHA partial-claim option is where FHA will pay the loan arrears to cure the delinquency, and then takes out a junior lien on the property for the amount of that payment. The promissory note associated with the lien bears no interest and is due-and-payable upon property sale.

<sup>f</sup> Also referred to as short sales, pre-foreclosure sales permit homeowners to engage in a normal marketing efforts for their properties, with an assurance the FHA will pay for any net shortages at settlement.

Source: US Department of HUD/FHA; October 2009.

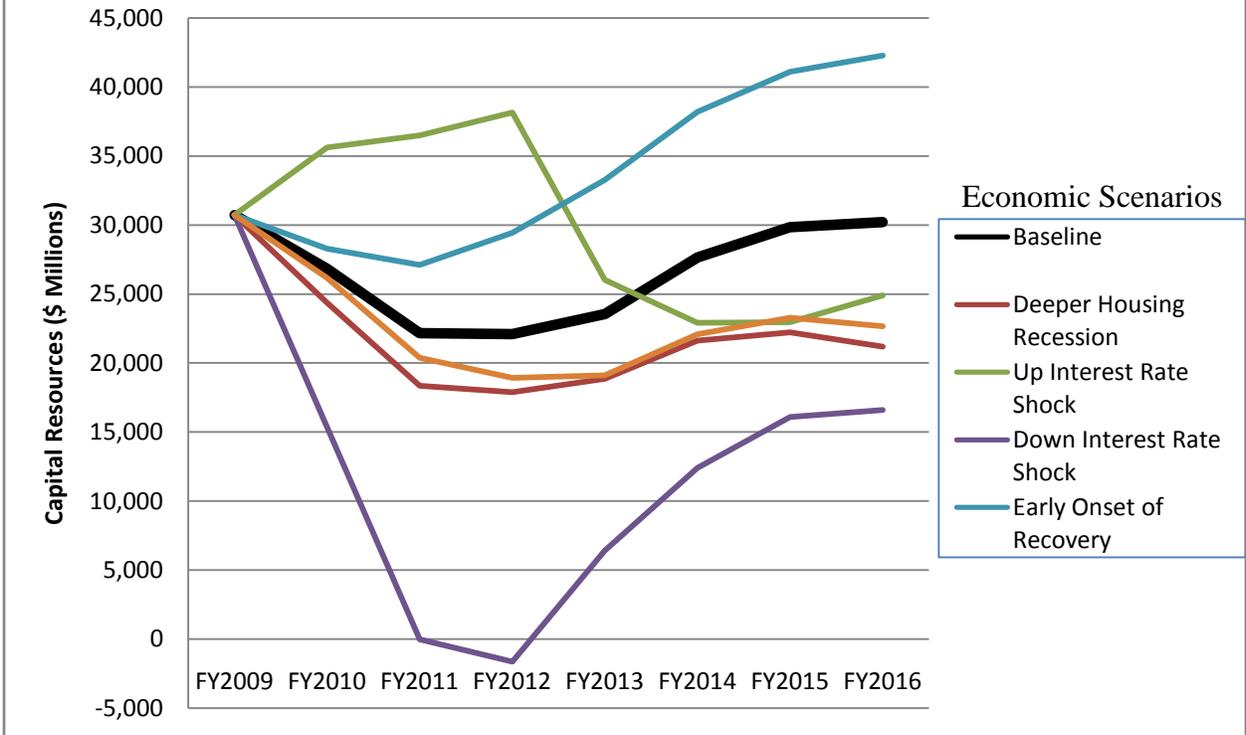
**Table 12. FHA Single-Family Insurance  
Claim Rate Experience of Loans with Seller-Funded  
Downpayment Assistance (DPA)  
as-of October 31, 2009**

Fiscal Year	DPA Endorsement Share <sup>a</sup>	DPA Claim Rate	Other Loans Claim Rate <sup>a</sup>	DPA Claim Rate Multiple
2000	1.74%	16.56%	7.26%	2.28
2001	4.92	17.30	6.47	2.67
2002	9.18	14.84	5.33	2.79
2003	18.40	14.02	4.68	3.00
2004	27.19	13.07	4.09	3.20
2005	33.09	12.42	4.41	2.82
2006	32.78	10.18	4.11	2.48
2007	35.09	6.91	2.59	2.66
2008	32.79	1.35	0.45	2.99

<sup>a</sup>Based upon home-purchase-loan insurance endorsements. Refinance loans are not included in this analysis.

Source: US Department of HUD/FHA; November 2009.

**Figure 1.**  
**Projected Capital Resources of the MMI Fund Under Various**  
**Economic Forecast Scenarios (\$ Millions)**



Source: MMI Fund actuarial studies for FY 2009; analysis by U. S. Department of HUD/FHA.