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Smooth Sailing for Multifamily Lending

Mandy Jackson

Fannie Mae and Freddie Mac remain active despite a restructuring of the two companies on the horizon

Multifamily has been good business for Fannie Mae and Freddie Mac and that is not expected to change, even though a restructuring of the two government- sponsored entities remains on the horizon.

The companies that back $5.1 trillion in home loans went into conservatorship last year, but reform appears to be far off in the distance as federal offi cials stay focused on problems in the residential mortgage market and broader economy.

Until it has a new plan, the multifamily industry continues to stay afl oat with competitive fi nancing from the two GSEs.

The Federal Housing Finance Agency placed Fannie Mae and Freddie Mac under conservatorship on Sept. 6 so that the regulator could control and oversee them until they are fi nancially sound and solvent, while conducting business as usual.

To facilitate their liquidity, the U.S. Department of the Treasury had planned to buy up to $100 billion each in preferred stock in Fannie Mae and Freddie Mac, purchase their mortgage-backed securities and extend a credit facility to the agencies.

Freddie Mac reported a net loss of $50.1 billion for 2008 compared to a 2007 loss of $3.1 billion.

The 2008 net loss at Fannie Mae was $58.7 billion after a $2.1 billion loss in 2007.

On May 8, Fannie Mae reported a fi rst-quarter 2009 loss of $23.3 billion, down from a $25.2 billion loss reported in the previous quarter.

Acting in its capacity as Fannie's conservator, the Federal Housing Finance Agency submitted a request on May 6 for $19 billion in federal aid from the Treasury Department.

On May 12, Freddie Mac reported a net loss of $9.9 billion for the fi rst quarter of 2009. The FHFA requested an additional $13.8 billion from the Treasury Department on Freddie Mac's behalf.

Since the fi rst of this year, Fannie Mae and Freddie Mac have requested $79 billion from the

U. S. Treasury under the stock purchase plan.

"The administration is utilizing Fannie Mae and Freddie Mac to assist in the resolution of the single-family mortgage problems that exist," said David Cardwell, vice president of capital markets and technology at the National Multi Housing Council in Washington, D.C.

Cardwell said the informal discussion of how to restructure the two GSEs is just beginning on Capitol Hill, but it is complicated by the fact that they have become implementers of the policies set out by the Obama Administration.

FHFA's conservatorship of Fannie Mae and Freddie Mac is scheduled to end at the end of 2009, but that timeline could be extended to deal with their existing mortgage portfolios as well as broader economic recovery activities. Both companies will need additional capital from the federal government to offset mortgage losses.

"They continue to source mortgage capital for apartments owners," Cardwell said.

"Without it, the multifamily industry would be in much worse shape." Still, GSE multifamily lending has fallen, though less than the decline in all commercial and multifamily lending, according to the Mortgage Bankers Association's most recent originations survey.

The dollar volume of multifamily loans by Fannie Mae and Freddie Mac decreased 17 percent in the fi rst quarter from fourth-quarter

2008. Overall, originations declined 26 percent for the same quarter.

Lowered Delinquencies All real estate is being impacted by the economy and property values have declined

across the board, including apartments, but the number of defaults remains low for Fannie Mae and Freddie Mac.

Between fourth-quarter 2008, the 60-day-plus delinquency rate on multifamily loans held or insured by Fannie Mae was 0.30 percent, according to the Mortgage Bankers Association.

The delinquency rate on multifamily loans held or insured by Freddie Mac that were 90 days or more past due was 0.01 percent.

Fourth-quarter delinquency rates were much higher for commercial mortgages held in commercial mortgage-backed securities at 1.2 percent and for commercial real estate loans held by banks and thrifts at 1.6 percent.

The delinquency rate for commercial mortgages held by life insurance companies was a low 0.07 percent.

Multifamily lending has always been a low-delinquency business for Fannie Mae and Freddie Mac, so it is unlikely that they will decrease their activity in that area, said Mark Riedy, executive director of the Burnham-Moores Center for Real Estate at the University of San Diego.

Riedy was president, chief operating offi cer and a director at Fannie Mae in the mid-1980s. He has also been an executive with the Mortgage Bankers Association, the Federal Home Loan Bank of San Francisco and the National Council of Community Bankers.

Riedy said it's politically diffi cult for the federal government to do anything that will change the structure of Fannie Mae and Freddie Mac.

Their roles as stockholder-owned institutions have already changed, but going forward they could be turned into federal government agencies or made into private companies that are so small they aren't "too big to fail." At the moment, those options appear to be in a stalemate.

Riedy said he doesn't know what the best structure would be for Fannie Mae and Freddie Mac.

He said government agency Ginnie Mae, created by Congress in 1968 in a manner similar to Fannie Mae and Freddie Mac, has done a good job of keeping delinquencies low despite the low downpayments for the home loans that it guarantees.

Ginnie Mae operates under the Department of Housing and Urban Development and backs mortgages made by the Federal Housing Administration and Department of Veteran Affairs.

"On the one hand, you could have a government corporation and then you wouldn't need two [companies] to take on conforming, non-FHA and -VA loans," Riedy said, "but it would be a huge government corporation and governments really haven't been the best to run major private-sector organizations."

On the other hand, the government doesn't want to inhibit the operations of Fannie Mae and Freddie Mac by splitting them into smaller companies because the mortgage market depends so heavily on them.

"I think they have to continue at least for the next several years to be a major player in the mortgage business," Riedy said. "They should continue to purchase mortgages on a conservative underwriting basis."

There has been some discussion that in five, 10 or 15 years, Fannie Mae and Freddie Mac might be broken into smaller regional companies that compete with each other. Riedy said it is likely that there will be a combination of approaches for restructuring the firms.

"The focus now is to get them on sound footing and make their securities marketable — and they will with government support," he said.

A spokeswoman for the House Financial Services Committee said the committee will hold hearings on Fannie Mae and Freddie Mac in the fall, but right now the committee is focused on mortgage reform and broader regulatory reform.

Since Fannie Mae guarantees $3.1 trillion in single-family mortgages and Freddie Mac backs $1.8 trillion in home loans, multifamily is a small part of their business in comparison.

Fannie Mae fi nanced $35.5 billion in multifamily housing in 2008, through debt fi nancing and bond purchases.

Freddie Mac invested $24 billion in multifamily housing last year through its whole loan and bond guarantee businesses and bought $1.4 billion in multifamily CMBS.

Jon Reible, senior vice president and western regional manager based in Phoenix for KeyBank Real Estate Capital, said Fannie Mae and Freddie Mac remain active nationwide.

A Smaller Piece of the Pie KeyBank did $337 million in lending in 2007 through Fannie Mae and Freddie Mac, representing 14 percent of all multifmaily loans. In 2008, the bank did $1.5 billion in lending through the GSEs — $650 million through Fannie Mae and $850 million through Freddie Mac — representing 43 percent of its multifamily lending.

While apartments are performing better in some markets than in others, Reible said the two companies continue to lend in markets with higher vacancy rates and less investment activity, but with more conservative underwriting.

"The activity itself is probably remaining relatively steady," he said. "It's just a smaller pie though and Fannie and Freddie are getting a much larger slice of that pie now."

Apartment buyers who normally seek fi nancing from life insurance companies and other balance sheet lenders are converting to Fannie Mae and Freddie Mac borrowers.

“With other capital sources drying up, it’s an opportunity to show what Fannie and Freddie can do and it sells very well,” Reible said.

Reible said it’s tough to compare Fannie Mae and Freddie Mac to other multifamily lenders, because there are so few other sources of capital in the marketplace.

“For a stabilized property with a good-quality sponsor, they are the lending source now,” he said.

“They will lend up to 70 percent to 80 percent of value based on the property and the strength of the borrower.” Interest rates from the two GSEs are 6 percent or lower for fi xed-rate fi nancing and 4 percent for floating-rate debt.

The vast majority of borrowers are opting for a fi xed rate, but some are taking on floating-rate loans so that they have prepayment fl exibility.

Most of the deals under consideration by Fannie Mae and Freddie Mac are for stabilized assets and most are refi nance transactions.

Apartment acquisitions slowed down a bit, but that business is starting to pick up in strong markets with good borrowers, Reible said.

Bill Rose, managing director in the San Diego offi ce of commercial mortgage brokerage Holiday Fenoglio Fowler LP, said life insurance companies and banks are interested in multifamily transactions in addition to Fannie Mae and Freddie Mac, but the two companies offer the best interest rates and non-recourse fi nancing.

Programs from the Federal Housing Administration and Department of Housing and Urban Development are best suited to fi nance acquisition and rehabilitation projects.

“The trouble that Fannie and Freddie has always been on the single-family side,” Rose said. “On the multifamily side, their underwriting has been pretty consistent.”

Investors in the apartment market have shifted to a long-term hold strategy, but Fannie Mae underwrites in-place rental rates rather than rents projected in future years, according to Heidi McKibben, vice president and head of multifamily production at Fannie Mae, who spoke on April 8 at the Millennium Biltmore in downtown Los Angeles during a multifamily conference hosted by the Casden Real Estate Economics Forecast from the University of Southern California’s Lusk Center for Real Estate.

“The good thing about this cycle is it is taking us back to realistic underwriting of real estate that will take us through the length of a 10-year loan,” said Timothy White, president of PNC ARCS, a Fannie Mae-delegated underwriting and servicing lender, at the Casden Forecast event.

“You have to look forward to an exit strategy and make sure you can refi nance it or it can be sold,” White said.

CREJ Staff Writer Keeley Webster contributed to this report.