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THE GSEs' FUNDING OF AFFORDABLE LOANS

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A. Introduction and Main Findings

An important issue highlighted by the recent affordable housing regulations for Fannie Mae and Freddie Mac and studies on the desirability of privatizing these two government-sponsored enterprises (GSEs) concerns the extent to which the GSEs lead or lag the overall mortgage market in financing affordable housing for disadvantaged borrowers. These GSEs receive substantial benefits from their Federal charters, mainly in the form of lower funding costs due to their "agency status". In exchange for their Federal benefits, they are required by Congress to promote access to mortgage credit for families and communities not being well served by the mortgage market, as well as to promote stability in the overall secondary market.

Both GSEs state that their loan purchases reflect the primary mortgage market's distributions across different income and racial categories of borrowers. That is, they believe that they are doing as good a job as other market sectors in funding historically underserved borrowers. For instance, in its 1995 report, "Financing Homes for a Diverse America", Freddie Mac concludes that the income and racial characteristics of borrowers whose loans it purchases are very similar to those of the overall conventional conforming market. Others, however, have reached different conclusions. Canner and Passmore (1995), HUD (1995, 1996) and Lind (1996a, b) report that the GSEs do not do as good a job as portfolio lenders in funding lower income borrowers and underserved neighborhoods.

This paper examines the GSEs' affordable lending performance using HMDA data on home purchase loans originated in metropolitan areas between 1992 and 1995. The data are drawn from the "FHA-eligible" portion of the conforming conventional market, in order to highlight the affordable sector of the housing market. The paper's main contribution is a more thorough treatment of data issues than provided by previous researchers.

Main Findings. The paper has seven main findings with respect to the GSEs' affordable lending performance.

(1) The shares of the GSEs' business going to lower income borrowers and underserved neighborhoods typically fall short of the corresponding shares of other market participants.

In 1995, very-low-income borrowers accounted for 17.3 percent of FHA-eligible loans retained in portfolio by depositories, compared with 12.4 percent of loans purchased by the GSEs, a 28 percent shortfall in performance. Census tracts where African Americans are more than 30 percent of the population accounted for 6.0 percent of depositories'

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retained loans, compared with 4.7 percent of the GSEs' loans, a 22 percent shortfall in performance. **(Section C)**

(2) The two GSEs show very different patterns of affordable lending. Fannie Mae is much more likely than Freddie Mac to purchase loans for underserved borrowers and for properties in their communities.

In 1995, African-American and Hispanic borrowers accounted for 14.6 percent of FHA-eligible home loans purchased by Fannie Mae, compared with 9.8 percent of such loans purchased by Freddie Mac. About 29 percent of Fannie Mae's loans funded properties in underserved neighborhoods (as defined by HUD) compared with 24.5 percent of Freddie Mac's loans. **(Section C)**

(3) Both GSEs have significantly improved their performance over the past four years. But Fannie Mae has improved its performance much more than Freddie Mac.

The share of Fannie Mae's purchases accounted for by very-low-income borrowers increased from 7.6 percent in 1992 to 13.0 percent in 1995. The corresponding increase for Freddie Mac was from 7.8 percent to 11.5 percent. **(Section C)**

(4) Fannie Mae's improvement has allowed it to narrow the gap between its affordable lending performance and those of other lenders in the conforming mortgage market.

In 1992, low-income census tracts accounted for 8.7 percent of Fannie Mae's purchases and 11.5 percent of all loans originated in the FHA-eligible conforming market; this translated into a "Fannie Mae-to-market" ratio of 0.76 (8.7/11.5). By 1995, the low-income tract percentages were 12.5 percent for Fannie Mae and 13.8 percent for the market, yielding a ratio of 0.91. There were similar increases in the Fannie Mae-to-market ratios for other socioeconomic categories examined in this study. In fact, in 1994 and 1995, Fannie Mae exceeded depository institutions in the share of its funding for Hispanic borrowers and for properties located in high-minority tracts, but continued to fall short of depositories on the other socioeconomic categories. **(Section D)**

(5) Freddie Mac's improvement, on the other hand, has not always been great enough to keep it in step with the conforming conventional market. In some cases, Freddie Mac's performance has actually declined relative to the market.

Between 1992 and 1995, the Freddie Mac-to-market ratio for very-low-income borrowers increased from 0.72 to 0.77 (versus 0.70 to 0.87 for Fannie Mae) However, for some other categories examined here, Freddie Mac's performance either declined relative to the overall market or showed only very slight improvement. For instance, the Freddie Mac-to-market ratio for underserved areas declined from 0.87 in 1992 to 0.82 in 1995, while

the ratio for African-American borrowers increased slightly from 0.66 to 0.69. **(Section D)**

(6) Because they are so large, the GSEs account for a significant share of the total FHA-eligible market. However, their market share for each of the affordable lending categories is less than their share of the overall market.

In 1995, it is estimated that the GSEs purchased 28 percent of all FHA-eligible home loans in metropolitan areas, but only 14 percent of all African-American loans and 22 percent of all loans financing properties in underserved areas. In contrast, FHA, which focuses mainly on credit-constrained borrowers, insured a smaller share of all FHA-eligible loans (25 percent) but much larger shares of African-American loans (41 percent) and underserved area loans (30 percent). **(Section E)**

(7) One surprising characteristic of the GSEs' lower income loan purchases is that they frequently do not appear to be addressing problems of affordability such as lack of cash for downpayments.

As reported in HUD's Privatization Study, almost 60 percent of the GSEs' purchases of very-low-income loans in 1995 had loan-to-value ratios less than 80 percent, compared with about 50 percent of their purchases of higher-income loans. The explanation for the seemingly large percentage of high-downpayment loans among the GSEs' lower income loan purchases requires further study. **(Section F)**

Overall, the HMDA data suggest that there is room for further improvement in the GSEs' performance, particularly the performance of Freddie Mac. The affordable housing goals, which are implemented by HUD, are designed to encourage the GSEs' to make that improvement and to narrow the gap between their performance and that of the overall market.

The findings from this and other studies present a very different picture of the GSEs' performance from that reported by the GSEs themselves. Since the various researchers are using similar data bases, it is surprising that the empirical findings are so different between the studies. Because these differences might be due to different ways of adjusting the data, Appendix A to this paper carefully describes how the HMDA data are treated in this study. Appendix B replicates the analytical tables for the entire conforming conventional market, that is, it incorporates "non-FHA eligible" loans into the analysis.

Because this paper uses aggregate (nationwide) data to compare the GSEs' with other market participants, it provides only a broad picture of trends in affordable lending. More disaggregated analyses both at the individual lender level and the regional and metropolitan area levels would be useful next steps.

B. Data Sources and Market Definitions

Data Sources. Since 1993, the GSEs have been providing HUD with annual loan-level data that includes detailed mortgage characteristics for all of their purchase transactions. This "GSE data base" is useful for analyzing the financial, borrower and locational characteristics of GSE loan purchases, for measuring changes in GSE performance over time, and for comparing Fannie Mae and Freddie Mac. This data base is used here to verify HMDA-reported data on GSE purchases.²

In order to compare the GSEs with the primary market, it is necessary to use HMDA data, which provides information on both primary market originations and secondary market purchases. Thus, HMDA allows comparisons of GSE performance with portfolio lenders such as banks and thrifts.

There are also a number of technical issues regarding the coverage and potential biases of HMDA data.³ These issues, which are noted throughout the discussion, are explained in Appendix A.

Market Definitions. Table 1 gives an overview of single-family lending as reported by HMDA for 1995. The GSEs purchase loans in the conforming conventional sector of the mortgage market, which in 1995 included all conventional (non-government) loans less than \$203,150. Table 1 presents separate data for the "FHA-eligible" portion of this market. FHA-eligible loans are conventional loans that fall within the FHA maximum loan limit for each metropolitan area, which is typically equal to 95 percent of each area's median house price.⁴ Thus,

² See Tables A.1 and A.2 in Appendix A for a comparison of the borrower and locational characteristics of GSE mortgage purchases as reported by HMDA and by the GSEs' own data. The two data bases yield similar distributions at the national level for the affordable lending categories examined in this study.

³ For example, HMDA reporters are only required to report the location of loans originated in metropolitan areas.

⁴ Specifically, in 1995, the FHA loan limit was 95 percent of the area median house price, subject to a minimum of \$78,660 and a maximum of \$155,250.

these loans are from the lower end of the market. Reflecting public interest in homeownership, this paper focuses on home purchase loans in the FHA-eligible sector of the conforming conventional market. As shown in Table 1, these loans account for about two-thirds of conforming conventional home purchase loans. For purposes of comparison, data covering the entire conforming market are reported in Appendix B.

The most appropriate comparisons for the GSEs are with the retained portfolios of depository institutions (banks and thrifts) also operating in the conforming market. However, data from other sectors, such as FHA and the Veterans Administration (VA), are often presented in order to provide a complete picture of the mortgage market. There has been a long-standing issue about whether conventional manufactured home loans should be included in market data that are being compared with GSE data. Because manufactured home loans generally do not meet the GSEs' underwriting standards, Fannie Mae and Freddie Mac have argued that manufactured home loans should not be considered in such comparisons. Similar concerns have been raised by the GSEs about below-investment-grade loans, or so-called "B&C" loans, which are also included in HMDA data. The tables below exclude from the conforming market totals loans by nine lenders that originate primarily manufactured home loans and loans by 42 lenders that originate primarily "B&C" quality loans.⁵ Because manufactured home and "B&C" loans are a growing source of affordable lending, the socioeconomic characteristics of these borrowers are provided as separate exhibits in some of the tables.

C. Borrower and Neighborhood Characteristics of 1995 Mortgages

Table 2 reports borrower and census tract characteristics of home purchase mortgages originated by various market segments in metropolitan areas during 1995. Each "distribution of business" percentage reported in Table 2 indicates the importance of a particular borrower or geographic subgroup in the mortgage lending activity of a market sector. For example, very-low-income (VLI) borrowers⁶ accounted for 12.4 percent of the GSEs' total purchases of FHA-eligible home loans originated in metropolitan areas in 1995. Corresponding figures for other categories were 5.3 percent for African-American borrowers, 7.5 percent for Hispanic borrowers,

⁵ See Appendix A for further discussion of these and other exclusions.

⁶ Those borrowers with incomes equal to or less than 60 percent of area median income.

11.7 percent for borrowers living in low-income census tracts, and 27.3 percent for borrowers living in underserved areas as defined by HUD's Geographically Targeted Goal.⁷

⁷ A metropolitan tract is underserved if the ratio of tract median family income is no more than 90 percent of area median family income or minorities comprise at least 30 percent of a tract's population and tract-to-area median family income does not exceed 120 percent.

The above percentages for the GSEs are difficult to interpret without similar data for either the overall market or specific market segments of interest. For example, comparable data for FHA reported in Table 2 indicates that 18.2 percent of FHA's borrowers had very low incomes, 15.3 percent were African American, 19.0 percent lived in low-income census tracts, and 40.7 percent lived in underserved areas. FHA's shares for these groups are much higher than the GSEs' shares, which means that affordable lending is a more important component of FHA's business than of the GSEs' purchases. This is not surprising, given that FHA's mission is to focus on the more credit-constrained borrowers purchasing a home for the first time. In 1995, two-thirds of FHA home purchase loans were for first-time homebuyers, compared with about 30 percent of loans purchased by the GSEs.⁸

Comparisons with Portfolio Lenders. Most FHA loans would not qualify for conventional financing, thus for the GSEs, the more relevant comparison is with the non-GSE portion of the conventional conforming market which consists mostly of portfolio lenders such as banks and thrifts. In general, loans sold to the GSEs in 1995 were less likely to be for disadvantaged groups than were loans retained by portfolio lenders, especially those held by commercial banks. For example, VLI borrowers accounted for 11.5 percent of loans purchased by Freddie Mac, 13.0 percent of loans purchased by Fannie Mae, and 19.0 percent of loans retained by banks. African-American borrowers accounted for 4.2 percent of loans sold to Freddie Mac and 6.0 percent of loans sold to Fannie Mae, compared with 6.8 percent of loans retained by banks. On the other hand, Hispanic borrowers accounted for a larger share of loans sold to Fannie Mae (8.6 percent) than loans retained by banks (6.4 percent).

The neighborhood data in Table 2 show similar differentials between the GSEs and banks. Low-income census tracts accounted for 10.2 percent of loans sold to Freddie Mac and 12.5 percent of sold to Fannie Mae, compared with 16.5 percent of loans retained by banks. High African-American neighborhoods⁹ accounted for 3.8 percent of Freddie Mac's loans and 5.3 percent of Fannie Mae's loans, compared with 6.6 percent of bank loans. However, when the neighborhood definition is changed to include all minorities (adding Hispanics and Asians), high-minority census tracts accounted for a larger proportion of the loans purchased by both Fannie Mae (17.4 percent) and Freddie Mac (15.6 percent) than of the mortgages retained by banks (15.0 percent).

⁸ The Department's Office of Policy Development and research recently completed a study of FHA's role relative to that of the GSEs and conventional lenders with affordable lending programs. It found that FHA underwriting and programs remained substantially more flexible when compared with the new conventional affordable lending initiatives and that FHA and conventional loans were made to significantly different types of borrowers. See Bunce et al. (1995).

⁹ High African-American neighborhoods are census tracts where African Americans account for over 30 percent of the tract population.

In general, the above comparisons show that the GSEs are not doing as good a job as portfolio lenders in funding disadvantaged borrowers and neighborhoods. Freddie Mac's affordable lending performance, in particular, stands out as lagging other sectors of the market. Fannie Mae funds disadvantaged borrowers and underserved neighborhoods at a much higher rate than Freddie Mac. In fact, Fannie Mae's performance in some instances approaches or exceeds that of the thrift industry (see Table 2).

Factors Explaining Portfolio Lenders' Performance. Some have offered reasons why portfolio lenders might serve disadvantaged groups better than the GSEs. Canner and Passmore (1995) point out that portfolio lenders have extensive knowledge of their communities, which they are able to utilize to manage credit risk. In addition, they may have direct interactions with their borrowers, enabling them to assess credit risk more accurately. These factors allow portfolio lenders to underwrite loans more flexibly than firms strictly following the GSEs' guidelines, which do not reflect this detailed knowledge. Secondary market firms such as the GSEs must set underwriting standards more strictly to compensate for the fact that they cannot directly evaluate risk.

Another important factor influencing the types of loans held by portfolio lenders is the Community Reinvestment Act (CRA), which requires depository institutions to help meet the credit needs of their communities. CRA provides an incentive for portfolio lenders to initiate affordable lending programs with underwriting flexibility, and the loans are often held in portfolio because they do not conform to the GSEs' underwriting standards.

These factors may explain why portfolio lenders are retaining more affordable loans than the GSEs are purchasing. However, in the 1992 GSE Act, Congress stated that it expected the GSEs to lead the industry in the financing of homes for lower income borrowers and for properties in underserved neighborhoods. Congress expected the GSEs to meet public purposes in return for the sizeable benefits that accrue to them from their Federal charters. To focus the GSEs' efforts on affordable lending, Congress established three housing goals for the GSEs and required that they submit annual reports to HUD on their performance with respect to these goals. HUD's recent privatization study showed that GSEs have significantly improved their affordable lending performance since the housing goals were first established (HUD, 1996). An important question is whether the GSEs have improved their affordable lending performance relative to that of other lenders, or whether their improvement has fallen short of the gains made by other lenders. Section D uses 1992-1995 HMDA data to answer this question.

D. Trends in Affordable Lending

During the 1990s the mortgage industry has markedly increased its outreach efforts and new products aimed at serving lower income and minority borrowers and their communities (Bunce, et al., 1996). The GSEs, along with private lenders and private mortgage insurers, have played an important role in this revolution in affordable lending. Fannie Mae and Freddie Mac

have developed special mortgage products such as the 97-percent loan-to-value mortgage and have entered into partnerships with local governments and nonprofit organizations to increase mortgage access to underserved borrowers. Even more importantly, the GSEs have modified their underwriting standards to address the needs of families who have found it difficult to qualify under traditional guidelines. For instance, they now allow loan approval based on "income stability," which helps lesser-skilled workers who, despite frequent job changes, manage to earn a steady income.

The HMDA data reported in Table 3 on trends in affordable lending suggest that the industry initiatives are working. The proportion of total mortgage lending going to lower income families and minorities increased substantially between 1992 and 1995. The share of loans going to very-low-income families, for example, increased from 10.8 percent to 14.9 percent during this period, an increase of 38 percent.¹⁰ Similarly, the share for African Americans and Hispanics increased from 8.3 percent to 13.3 percent, an increase of 60 percent. While low interest rates, income growth and moderate house price inflation made homeownership very affordable during this period, most observers think that the new industry initiatives were also an important factor explaining the substantial improvement in lending to lower income and minority families.

GSEs Relative to Depositories. Both the GSEs and the depositories (banks and thrifts) improved their affordable lending performance between 1992 and 1995. The data reported in Table 3 show that Fannie Mae has significantly improved its affordable lending performance relative to depositories, which is consistent with the many special programs that Fannie Mae has initiated over the past few years. For example, in 1992, very-low-income borrowers accounted for 7.6 percent of Fannie Mae's home loan purchases and 14.0 percent of home purchase loans retained by depositories, for a "performance ratio" of 0.54 (7.6/14.0). By 1995, this "Fannie Mae-to-depositories" ratio for VLI borrowers had risen to 0.75 (13.0/17.3) -- that is, Fannie Mae's performance had increased from 54 percent to 75 percent of the depositories' performance.

Freddie Mac also improved its performance relative to the depositories, but not nearly as much as Fannie Mae. While Freddie Mac's VLI percentage (7.8 percent) was approximately the same as Fannie Mae's in 1992, its VLI percentage increased to only 11.5 percent by 1995. In other words, the "Freddie Mac-to-depositories" ratio for VLI borrowers increased from 0.56 in 1992 to 0.66 in 1995, but Fannie Mae's ratio increased from 0.54 to 0.75 over the same period.

¹⁰ Note that the percentages for very-low-income borrowers declined from 16.2 percent in 1994 to 14.9 percent in 1995. This reduction between 1994 and 1995 may be partially due to our updating the definition of the FHA-eligible market with revised (and higher) FHA loan limits that took effect in 1995. However, this effect is likely small given that the comparisons in Table B.2 for the entire conforming market (which are not affected by the FHA-eligible loan limits) also show slight declines in very-low-income lending. This point applies as well to the other variables listed in Table 3.

GSEs Relative to the Conforming Market. Table 3 reports in parentheses changes in the GSEs' performance relative to the overall conforming conventional market. As noted earlier, some expect the GSEs to lead the conforming market in funding affordable loans. The conclusions remain the same as discussed above for Fannie Mae -- the share of Fannie Mae's purchases going to lower income and minority borrowers and their neighborhoods has increased relative to the corresponding shares for the overall market. Fannie Mae's recent improvement has significantly reduced the gap between its performance and that of the market, although in 1995 it continued to lag the market and depository institutions on important dimensions of affordable lending.

Freddie Mac's recent improvement, on the other hand, has not been large enough to significantly reduce its affordable lending gap relative to the conforming market. For several socioeconomic categories examined here, Freddie Mac's performance either declined relative to the market or showed only very slight improvement. For example, the "Freddie-Mac-to-market" ratio for low-income census tracts declined from 0.80 in 1992 to 0.74 in 1995, while the ratio for African-American borrowers increased slightly from 0.66 to 0.69 (see Table 3).

To summarize, Freddie Mac has improved its performance relative to depository lenders but has not improved its performance relative to the overall conforming market.¹¹ Fannie Mae has improved its performance relative to both depositories and the overall market. By 1995, Fannie Mae's performance either exceeded or was close to the market on several categories (e.g., Hispanic and African-American borrowers, high-minority tracts, underserved areas); however, Fannie Mae's performance continued to fall significantly short of portfolio lenders, especially commercial banks, on most dimensions of affordable lending. Freddie Mac's 1995 performance fell short of both portfolio lenders and the overall conforming market on all dimensions of affordable lending.

E. Market Share Data for 1995

Even if a high percentage of a market sector's business is made to a particular disadvantaged group, it is not necessarily true that the sector plays a major role in funding mortgages for that group. The absolute size of the market sector must also be taken into account in order to determine the sector's "market share of total lending" to a disadvantaged group.

The "distribution of business" comparisons between FHA and the GSEs did not take into account differences between the number of loans purchased by the GSEs and the number of loans insured by FHA. Because the aggregate volume of GSE business significantly exceeds that of FHA, in some cases the absolute numbers of loans of various types purchased by the GSEs are actually greater than the corresponding numbers of loans insured by FHA. For example, in 1995, first-time homebuyers accounted for 70 percent of FHA's business but only 30 percent of the

¹¹ The reason for this is the large improvement made by Fannie Mae which impacts the trend data of the overall market.

GSEs' business. However, in 1995 the GSEs purchased more first-time homebuyer loans than FHA insured.¹²

¹² In 1995 Fannie Mae purchased 258,000 loans made to first-time homebuyers (32 percent of its home purchase loans) and Freddie Mac purchased 159,000 such loans (30 percent of its home purchase loans), yielding a GSE total of 417,000 loans for first-time homebuyers -- 24 percent more than FHA's 317,765 first-time homebuyer loans.

The "market share" data reported in Table 4 measure the importance of the GSEs in the funding of lower income families, minorities, and underserved areas, by dividing the number of GSE loan purchases for each subgroup by total market originations for that subgroup.¹³ In this section, the market is defined as all FHA-eligible home purchase mortgages in metropolitan areas.¹⁴

In 1995, it is estimated that the GSEs purchased 28 percent of all FHA-eligible loans and 14-23 percent of loans in the affordable lending categories listed in Table 4. These data show that the GSEs' overall market share is larger than their market share for each of the affordable lending categories. The situation is reverse for FHA. FHA insured 25 percent of all FHA-eligible loans and 29-41 percent of loans in the affordable lending categories. For example, FHA insured 41 percent of all loans for African American borrowers and 30 percent of loans financing properties in underserved areas. The GSEs, on the other hand, purchased only 18 percent of African-American loans and 22 percent of underserved area loans.

F. High Downpayments on GSEs' Lower income Loans

Lower income families are constrained from becoming homeowners because their incomes limit the monthly mortgage payment for which they can qualify and also make it more difficult to accumulate enough cash for a downpayment. Surprisingly, the GSE data indicate that lower income borrowers do not have a greater preponderance of relatively low-downpayment mortgages despite the difficulty of accumulating a downpayment. As reported in HUD's recent privatization study, lower income loans purchased by the GSEs have a greater percentage of low loan-to-value ratios than the higher income loans that the GSEs purchase.

¹³ Market share numbers do not reflect the actual risk borne by the GSEs since many affordable loans have private market insurance. See Canner and Passmore (1995) for a discussion of credit risk borne by the GSEs.

¹⁴ Specifically, the market includes FHA-insured mortgages, loans guaranteed by the Veterans Administration (VA), and all FHA-eligible conforming conventional loans (including mobile home and B&C loans). As explained in Appendix A, the market share figures reported here are estimates and depend on assumptions about under-coverage of HMDA data. Readers interested in market shares including non-FHA-eligible conventional loans, see Table B.3 in Appendix B.

In 1995, 58 percent of very-low-income borrowers had loan-to-value ratios (LTVs) less than 80 percent, compared with less than 50 percent of borrowers from other income groups (HUD, 1996).¹⁵ In addition, a surprisingly large percentage of the GSEs' first-time homebuyer loans have had high downpayments. In 1995, 35 percent of Fannie Mae's and 41 percent of Freddie Mac's first-time homebuyer loans had downpayments of 20 percent or more.¹⁶ Essentially, the GSEs have been purchasing lower income and first-time homebuyer loans with large downpayments.

HUD data show that over two-thirds of FHA-insured home purchase loans have an LTV ratio greater than 95 percent. But as noted earlier, the more relevant comparison for the GSEs is with portfolio lenders in the conforming market. Lower income loans retained in portfolio by banks and thrifts may also have low LTV ratios, similar to those purchased by the GSEs. Unfortunately, data on both income and LTV are not readily available for the depository institutions, as they are from the loan-level data that the GSEs report annually to HUD. The HMDA data, which includes borrower incomes for depository loans, does not include LTV ratios. HUD has initiated research on this issue using other mortgage market data sources such as the American Housing Survey.

G. Conclusions and Caveats

The HMDA data show clearly that the GSEs lag other market sectors in the share of their funding for affordable loans. The GSEs have improved their performance, but there is room for further improvement, particularly for Freddie Mac. Freddie Mac lags both Fannie Mae and depositories in funding loans for underserved borrowers and has only slightly improved its relative position in the affordable lending market over the past few years. The affordable housing goals, which have been established by HUD, are designed to encourage both GSEs to make improvement and narrow the gap between their performance and that of the overall market.

Caveats. Some caveats that must be kept in mind when interpreting the data presented in this report include:

(1) The GSEs have used similar data (HMDA and the GSE loan-level data) and reached almost the opposite conclusions as ours. Therefore, when reviewing studies such as this, one must pay particular attention to the methods and assumptions used by the researchers to adjust the data. Appendices A and B describe how HMDA data have been treated in this study and present alternative definitions of the mortgage market.

¹⁵ Twenty nine percent of very-low-income borrower loans had LTVs above 90 percent, which was similar to or less than the percentage of over-90-percent-LTV loans for other income groups.

¹⁶ For information on the GSEs' loan-to-value ratios, see HUD, 1996, p. 99.

(2) There are different viewpoints about the types of loans that should be included in analyses such as this. Some sectors are important sources of affordable lending that possibly should be excluded from comparisons with the GSEs. For example, it may be inappropriate to compare the FHA with the GSEs because the FHA is government-owned with a specific mandate to serve the most credit-constrained borrowers. That is why we focus on comparisons of the GSEs with portfolio lenders in the conventional market.

The GSEs believe that manufactured home loans should be excluded from comparisons with them because only a small portion of these loans meet their underwriting standards. We have excluded data for nine manufactured home lenders from our comparisons but have included them as a separate exhibit in Table 2 to highlight that industry's important contribution to affordable housing. In addition, there are some manufactured home loans that satisfy the purchasing guidelines of the GSEs.

A similar issue surrounds "B&C" loans. As explained in Appendix A, we excluded from our analysis 42 lenders that originate primarily B&C loans. The GSEs have argued that B&C loans originated and retained by depositories should also be excluded from comparisons with their purchases because those loans are not "investment grade". Data are not available to separate depository loans according to investment grade.

Still, it is appropriate to compare the total inventory of retained depository loans with the loans purchased by the GSEs. Both sectors receive Federal benefits and their relative efforts in the affordable lending area are a topic of interest to policy makers. As discussed earlier, the fact that one can explain why depository institutions are doing a better job funding affordable loans than the GSEs does not mean that the situation should stay the same. Some think that the GSEs should be doing a better job than the depository institutions (that is, "leading the industry") because of the enormous benefits that they accrue from their Federal charters.

(3) This paper uses nationwide data to compare the GSEs with other market participants. Thus, it provides only a broad picture of trends in affordable lending. More disaggregated analyses both at the individual lender level and at the regional and metropolitan area levels are needed to fully understand the differences between GSE purchases and loans retained in portfolio.¹⁷

¹⁷ See for example, Lind (1996a, b).

APPENDIX A

HMDA METHODOLOGY

This appendix discusses issues involved when using Home Mortgage Disclosure Act (HMDA) data to compare primary and secondary market funding of affordable loans.¹⁸ In particular, we discuss HMDA's coverage of mortgage market activity, the role of mortgage company subsidiaries, and loans that are excluded from the analysis.

A. HMDA Coverage

HMDA data is the most comprehensive source of information on primary mortgage market originations and secondary market loan purchases. HMDA provides information on the borrower (income, race and ethnicity, and sex) and locational (census tract, metropolitan area) characteristics of lending institutions' originations and purchases of mortgages.¹⁹ However, HMDA is not a complete census of mortgage origination and secondary market activity in the United States. HMDA data is only required for lenders that originate loans for properties in metropolitan areas.²⁰ In addition, some metropolitan lenders are exempt from HMDA reporting requirements.²¹

¹⁸ The authors are currently working on a more complete discussion of these issues. For other discussions about the scope and coverage of HMDA data, including its major gaps, see Avery, Beeson, and Sniderman (1994 and 1995), Yezer (1995), Horne (1994), Canner and Gabriel (1992), Canner and Passmore (1995) and Canner and Smith (1991 and 1992).

¹⁹ HMDA was enacted in 1975 in response to Congressional concerns that depository institutions (mainly banks, thrifts and their subsidiaries) were not adequately serving low-income and high-minority neighborhoods. HMDA required these institutions to report annually their mortgage lending by census tract location; with this information, the public could assess whether banks and thrifts were adequately serving their communities. HMDA reporting was expanded in 1990 to provide information on the disposition of loan applications (i.e., approved and accepted, approved but not accepted by the borrower, denied, withdrawn, or not completed), to include activity of large independent mortgage companies, and to provide information on the race and income of individual loan applicants. These data were needed to assist in the detection of lending discrimination. Finally, an additional expansion in 1993 covered mortgage companies that originated 100 or more home purchase loans in the preceding calendar year.

²⁰ HMDA does include a small number of mortgage originations for properties in non-metropolitan areas but most of these loans are either manufactured home loans or loans located in areas that are adjacent to a metropolitan area. A significant number of HMDA loans do not include any geographic identifiers.

²¹ Loans financed by non-profit groups and consortiums of lenders are not likely to be reported under HMDA. State Housing Finance Agencies (HFAs) are another source of affordable lending. HFA-financed mortgages are likely reported under HMDA by the lender that originates these loans.

This section discusses three issues that could affect HMDA's coverage of primary and secondary market activity -- under-reporting of mortgage originations by brokers and correspondents, missing data on borrower characteristics, and under-reporting of GSE purchases. Under-reporting of mortgage activity by HMDA could affect the calculation of our "distribution of business" and "market share" estimates.

A.1 Brokered and Correspondent Loans

This paper assumes that the total market for conforming loans in metropolitan areas includes only originations reported to HMDA. It was noted earlier that some mortgage originations may not get reported in HMDA at all. In addition, there are some newly originated mortgages that may get reported as a purchase - e.g., some brokered and correspondent loans may not get reported under HMDA as originations but as purchased loans. Loan originations must be reported by the institution that makes the credit decision and, by prior agreement, acquires the loan after closing. On one hand, if a loan is closed in a correspondent or broker's name without prior agreement for resale to another institution, then the correspondent or broker is subject to the same reporting requirements as other non-depository institutions. On the other hand, if a broker or correspondent closes a loan in the name of an affiliate lending institution, then the affiliate should report the loan as an origination. It is possible that a broker or correspondent closes a loan in the name of an affiliate lending institution but the lending institution treats the loan as a loan purchase rather than as an origination.²² These loans would not be included in HMDA as originations.

Our focus on mortgage originations assumes that the majority of secondary market purchases reported by HMDA lenders have also been reported to HMDA as originations. We base this assumption on an analysis that matched origination records for loans that were reported as sold with loan purchase records for the Washington D.C. metropolitan area.²³ A substantial

²² *Inside Mortgage Finance* (September 6, 1996) reports that correspondent and broker loans are generally not reported as originations but as loan purchases under HMDA. They report that HMDA numbers are within one percent of originations reported by HUD after counting loan purchases as originations. Federal Reserve staff, on the other hand, claim that including purchased loans leads to double counting since the majority of these loans have also been reported to HMDA as loan originations.

²³ We used the matching technique described in Canner and Passmore (1995). Canner and Passmore used this technique to match private mortgage insurance data with HMDA data.

number of loan purchases were matched with loan originations suggesting that counting loan purchases as originations leads to double-counting.

A.2 Missing Data

A lender may be required to comply with HMDA but may not be required to report all the borrower and locational information about the loan.²⁴ Missing data makes it more difficult to evaluate the affordable lending behavior of primary and secondary market participants, since we cannot determine whether loans are for low-income or minority borrowers or borrowers located in low-income neighborhoods. For the distribution of business and market share estimates reported in this paper, we exclude loans with missing data from our calculations.²⁵

A.3 Under-reporting of GSE Purchases

²⁴ A depository institution need not report borrower race, sex, or income if it has assets of \$30 million dollars or less. A lender is not required to request race information if the application is taken by telephone. If an application is received by mail, the lender must request race information, but the borrower does not have to provide it. Lenders need not report borrower income, sex, or race for loans purchased from other lending institutions. A lender does not report borrower income information if it does not take income into account when making the credit decision (e.g., FHA streamline refinance loans.) Lenders need not geocode loan application data for properties located in metropolitan areas in which it does not have a home or branch office or for properties in non-metropolitan areas.

²⁵ The effect of excluding loans with missing data from the distribution of business estimates is equivalent to assuming that missing data is distributed in the same way as loans without missing data. The effect of excluding loans with missing data from market share estimates depends on the relative amount of missing data for each market participant. For example, if FHA and GSE data have proportionately the same amount of missing data then market share comparisons between FHA and GSE will be unaffected.

GSE purchases include Fannie Mae and Freddie Mac purchases of primary market originations as well as loans purchased by a lending institution and then resold to either Fannie Mae or Freddie Mac.²⁶ Comparisons of HMDA data with the GSEs' loan level data show that HMDA's coverage of GSE purchases of home purchase loans was about 78.9 percent in 1994 and 84.7 percent in 1995. This section discusses issues specific to the under-reporting of secondary market activity by HMDA.

²⁶ Some of the loans reported as purchased by lenders may be seasoned loans (i.e., loans purchased in a year after the origination year).

Type of Secondary Market Purchaser. Lenders are required to report to HMDA whether they hold an originated or purchased loan in portfolio or sell the loan on the secondary market during the calendar year. For loans sold on the secondary market, HMDA lenders are required to report the type of purchaser.²⁷ Lending institutions may not accurately report a sale of a loan to a secondary market participant. In 1995, two of the largest lenders, Countrywide and Prudential, reported very few loans sold to the GSEs.²⁸ These lenders stated that they had recently changed their data systems and these systems had failed to correctly account for these loan sales. We noticed similar patterns for other major lenders for 1993-1995 HMDA. After calling 50 of the top major lenders that appeared to misreport loan sales²⁹, we conclude that HMDA's coverage

²⁷ The four main types of secondary market purchasers of conforming conventional mortgages include Fannie Mae and Freddie Mac, affiliates of the lender, and other purchasers such as non-affiliated institutions or pension funds.

²⁸ Countrywide and Prudential submitted corrected data for the "Type of Purchaser" field before the tape release of the 1995 HMDA data. The CD ROM version of the 1995 HMDA data, however, does not contain the corrected data. Countrywide and Prudential had reporting errors for only the "Type of Purchaser" field for 1995 data.

²⁹ Most of the lending institutions that misreport loan sales are independent mortgage companies. There are three major reasons for the misreporting of loan sale data. First, lenders reported that their HMDA reporting and secondary market data systems were not properly coordinated and loan sale information on their HMDA records was not refreshed when the loan was subsequently sold. Second, RATA, a major HMDA reporting software and data collection vendor, handles the HMDA reporting for many smaller lenders. If these lenders

of secondary market activity is incomplete because some lenders do not accurately report loan sales.³⁰

do not inform RATA of a loan sale then it does not get reported to HMDA. Finally, reporters that do not sell servicing rights sometimes do not report that the loan was purchased.

³⁰ Analysis of HMDA data also suggests that the sale of loans may not be properly reported by independent mortgage companies and depositories' mortgage company subsidiaries. These lending institutions reported a significant number of retained loans that they originated but did not sell in the calendar year, even after excluding loans originated in the last two months of the year that may still be in the warehouse pipeline. For example, independent mortgage companies reported that they retained 20,178 (or 7.7 percent) of their mortgage originations in 1995.

End-of-Year Originations. This paper's estimates do not adjust for loans that were originated during the last two months of the year and were not sold on the secondary market before the end of the year. Prior to 1995, HMDA's coverage of GSE purchases increases if we adjust for the end-of-year mortgages that may have not made it through the pipeline on their way to the secondary market.³¹ In 1995, HMDA's coverage of GSE purchases decreases if we exclude end-of-year mortgages. HMDA's coverage of Fannie Mae purchases decreases from 90.6 to 83.9 percent and HMDA's coverage of Freddie Mac purchases decreases from 76.3 to 70.3 percent.³² The reason for the decrease in coverage is HMDA's over-reporting the sale of mortgages in the last two months of the origination year. For example, HMDA reports Freddie Mac purchases to be 1.53 times Freddie Mac's actual purchases and HMDA reports Fannie Mae purchases to be 1.90 times Fannie Mae's actual purchases. HMDA's over-reporting of GSE purchases may be due to some lenders reporting commitments to sell loans to the GSEs in the following year, as current-year sales to the GSEs.

B. Implications of Under-reporting for Distribution of Business and Market Share Estimates

As discussed, HMDA reports include only 75-85 percent of GSE purchases in metropolitan areas. Comparisons of HMDA and FHA loan-level data show that HMDA accounts for approximately 80 percent of FHA originations. This section discusses the implications of this under-reporting for our distribution of business and market share estimates. HMDA under-reporting would not affect the distribution of business data if the unreported and missing data are not disproportionately concentrated in the affordable lending categories. Similarly, the market share data may not be biased if loans of different types are equally under-reported under HMDA.

Distribution of Business. We have compared the borrower and census tract distributions of GSE purchases derived from HMDA data with the corresponding distributions derived from the GSEs' own loan-level data, and the two distributions, at the national level, are quite similar.³³

³¹ Canner and Passmore (1995) excluded loans originated in the last two months of the year, reflecting the average lag between origination and purchase by the GSEs.

³² The deadline for submission of HMDA data is March 1. Although lending institutions have sufficient time to report the sale of loans originated in the previous year, HMDA requires that the sale be in the calendar year of the origination year for loans to be reported as sold. Hence, even if the institution knows that a loan has been sold, it does not report the sale unless it occurred before December 31. It is possible that some of the end-of-year originations show up as loan purchases in the following year.

³³ When comparing GSE loan-level data with HMDA data, HUD is only able to report publicly tables that have been derived from the public use version of the GSE loan-level data base. The public use data base that includes geographic identifiers does not distinguish between GSE purchases of home purchase and refinance mortgages, GSE purchases of owner and investor mortgages, and GSE purchases of FHA and conventional mortgages. With respect to the latter, Fannie Mae purchased about 9,500 FHA loans in 1995 while Freddie Mac purchased less than 100 FHA loans. Thus, the "GSE Data" reported in Tables A.1 and A.2 includes all

As shown in Table A.1, the HMDA-reported and GSE-reported distributions of GSE purchases of very-low-income and low-income loans have differed, on average, by less than one percentage point for 1994 and 1995. For example, HMDA data indicates that 19.2 percent of Freddie Mac's purchases in 1995 were low-income loans, above the 18.5 percent based on Freddie Mac's loan-level data.

The distributions for African-American and Hispanic borrowers given in Table A.1 are even closer than those for borrower income. For example, loans for African Americans accounted for 3.4 percent of Freddie Mac's 1995 purchases, compared with 3.6 percent based on Freddie Mac's loan-level data.

Table A.2 compares the census tract distributions derived from the HMDA and GSE data. In most cases, the differences between the data bases are rather small for the percentages of GSE purchases in low-income, African-American, Hispanic, and minority census tracts, and in underserved areas as defined for HUD's Geographically Targeted goal. For example, loans financing properties in underserved areas accounted for 21.1 percent of Freddie Mac's 1995 purchases based on HMDA and Freddie Mac's own loan level data.

Market Share. The market share estimates in Table 4 are based on HMDA data, which means that they assume that FHA, conventional conforming loans, and GSE purchases are equally under-reported by HMDA. Because of uncertainty about HMDA coverage, other assumptions were also examined. The results were robust with respect to changes in assumptions. For example, similar results were obtained using the GSE loan-level data to determine the number of GSE purchases and adjusting the FHA and conforming market numbers by 1.25 and 1.11 to reflect HMDA coverage ratios of 80 and 90 percent, respectively. The GSE market share estimate was calculated as the mid-point of estimates based on these two assumptions about HMDA coverage of FHA and conforming market loans. The estimated market shares were similar to those reported in Table 4.

C. Depositories' Mortgage Company Subsidiaries

these mortgage types. The "HMDA Data" reported in Tables A.1 and A.2 includes GSE purchases of owner and investor home purchase and refinance conventional mortgages but does not include GSE purchases of FHA loans. If FHA loans were excluded from the "GSE Data", thus making it comparable with the "HMDA Data", the results would not change much, except that Fannie Mae's HMDA-GSE differences would decline (in an absolute sense) for very-low-income and low-income borrowers.

Comparisons between the primary and secondary markets with respect to affordable lending must take into account the type of institution that ultimately holds (or funds) the loan. We have already identified several reasons why it is not easy to determine this from HMDA data (e.g., lending institutions do not accurately report loan sales).

Identification of the lending institution that funds a loan also depends on how we treat the originations of mortgage company subsidiaries. In this paper, we do not distinguish between a depository and its subsidiary when calculating distribution of business and market share estimates - i.e., depository loans include loans originated and held by depositories or their mortgage company subsidiaries.

Mortgage company subsidiaries do not sell all originations to their parents. Fannie Mae and Freddie Mac purchase the majority of mortgage company subsidiary loans. For example, in 1995 mortgage company subsidiaries of commercial banks reported 273,359 FHA-eligible conforming conventional home purchase originations, of which 36.0 percent were sold to Fannie Mae and 22.4 percent were sold to Freddie Mac.

Mortgage company subsidiaries of banks report that 18.1 percent of their loans are not sold. These loans are most likely loans that are still in the pipeline and have not been sold to the parent or an unaffiliated secondary market purchaser, or loans that the lender fails to report as sold on the secondary market.

Loans reported as held by mortgage company subsidiaries are likely a mixture of loans sold to parents and the GSEs. For example, HMDA reports (see Table A.3) that 15.2 percent of loans originated and retained by mortgage company subsidiaries of banks are for very-low-income borrowers which is much less than the 19.2 percent of loans originated and retained by banks. Thus, by including loans that are reported as held by mortgage company subsidiaries, we are probably underestimating the percentage of depositories' retained portfolios that are funded for affordable housing borrowers.

Our depository estimates are based only on loans originated and held by depositories and their mortgage company subsidiaries. We do not adjust our estimates for the loans that depositories purchase from their mortgage company subsidiaries. We could adjust our estimates in two ways. On one hand, we could calculate the distribution of business estimates for depositories based upon their retained originations and the loans that they purchase and hold in portfolio. Loans that are purchased by depositories and reported as not sold in the given year are more likely to be affordable housing loans than the loans originated and retained by depositories. For example, 19.9 percent of originations retained by commercial banks versus 22.3 percent of the loans purchased and retained by commercial banks are for very-low-income borrowers (see Table A.3).

On the other hand, we could calculate the distribution of business estimates based upon depository originations that are retained in portfolio and the mortgage company subsidiary's originations that were reported as sold to an affiliate. From Table A.3 we conclude that these

loans are more likely to be affordable housing loans - 23.0 percent were loans for very-low income borrowers - than loans originated and held by commercial banks.

Thus, either adjustment would lead to a higher percentage of affordable loans being reported for depositories.

D. Additional Loans Excluded from the Analysis

This section discusses loans excluded from the distribution of business and market share analyses because of errors in data reporting or because the GSEs generally do not purchase these loans.

High Loan-to-Income Ratios. A significant number of HMDA loans have high loan-to-income ratios. The reason for high loan-to-income applications is unclear.³⁴ We excluded these loans from our analysis when calculating borrower income distributions.³⁵ The reductions in the percentage of very-low-income borrowers from excluding these loans are reported in Table A.4.

Excluding high loan-to-income loans has substantial impact on the income distribution of GSE purchases in 1994. For example, the percentage of purchases of loans for very-low-income borrowers decreases from 11.0 to 9.4 percent for Fannie Mae and from 11.4 to 7.8 percent for Freddie Mac. After excluding these loans from 1994 HMDA data, the borrower income distribution for GSE-purchased loans more closely matches the income distribution obtained from Fannie Mae and Freddie Mac's loan-level data. For example, Freddie Mac's own data for 1994 is much smaller than the 11.4 percent figure that unadjusted HMDA reports. Thus, these high loan-to-income mortgages appear to be data errors in HMDA.³⁶

The percentages are not so dramatic in 1995. The very-low-income percentages for commercial banks and Fannie Mae are each reduced by 0.5 percent while Freddie Mac's very-low-income percentage is reduced by 1.1 percent.

Loans with Small Loan Amounts. We excluded loans with loan amounts less than \$15,000. These loans may be home improvement loans secured by first liens. If a home improvement loan is secured by a first lien, the lender has the option to report the loan as a home purchase loan rather than a home improvement loan. There are not many GSE purchases with

³⁴ Canner and Passmore (1995) conclude that a portion of these loans may be loans for older borrowers with relatively high wealth-to-income ratios or for young borrowers with high future income potential.

³⁵ We excluded loans from the analysis with loan-to-income ratios above six while Canner and Smith (1994, 1995) excluded loans with loan-to-income ratios above four.

³⁶ For example, one error may arise if lenders report monthly, instead of yearly, borrower incomes.

loan amounts less than \$15,000 reported under HMDA. However, a significant number of small loans are originated and held by commercial banks or their mortgage company subsidiaries. Not surprisingly, a large percentage (33.5 percent in 1995) of these loans are originated for very-low-income borrowers. Table A.5 reports the percentage of commercial bank (and bank mortgage company subsidiary) loans that were originated for very-low-income borrowers and not sold on the secondary market. Excluding these loans reduces the percentage of commercial bank loans originated for very-low-income borrowers by at least 1.6 percentage points for each year between 1993 and 1995.

Manufactured Home Loans. Manufactured homes are increasingly becoming an important source of affordable housing. Because of the nature of manufactured housing, the underwriting guidelines of lenders and the GSEs have often precluded the origination of these loans as mortgage loans. For the most part, manufactured homes are financed with personal finance loans and are not included in HMDA data. We have identified nine national lenders for manufactured housing loans.³⁷ In 1995, HMDA reported that these nine lenders originated 110,514 loans in metropolitan areas. We believe that these account for most of the manufactured home loans reported under HMDA.

The importance of manufactured homes as a source of affordable housing is shown in Table 2 and Table B.1. Almost half of these loans are for low-income borrowers. Only 13 percent of these loans are for African-Americans and Hispanics compared with 29 percent of FHA's loans. Excluding manufactured housing loans from the analysis does not change the comparisons between depositories and the GSEs, because both groups fund very few manufactured housing loans. Excluding manufactured housing loans, however, reduces the percentage of 1995 conforming conventional loans originated for very-low-income borrowers from 11.3 percent to 10.2 percent.

Manufactured housing will continue to increase its share of the housing market because of its affordability, new designs and amenities that compete well with traditional structures, and

³⁷ The nine lenders are Greentree Financial Corporation, Bank of America, FSB, Vanderbilt Mortgage, Oakwood Acceptance, Security Pacific, CIT Group, Washington Mutual, FSB, and SouthTrust Mobile Services. According to the Manufactured Housing Institute, Greentree Financial Corporation originates between 25 and 33 percent of manufactured housing loans.

HUD regulations that ensure the safety of these structures. Moreover, capital markets have begun to recognize the profitability of these loans.³⁸ Increasingly, more of the manufactured homes will qualify as property loans under primary and secondary market underwriting criteria.³⁹

³⁸ Greentree Financial Corporation, in particular, has been very successful in attracting investors for securities backed by its manufactured home loans.

³⁹ Trends in manufacturing home industry are discussed in "The Mortgage Lending Sleeper is Waking Up in Manufactured Homes," *Secondary Marketing Executive*, October 1996.

B&C Loans. B&C or below-investment grade lenders are also making an important contribution to affordable lending. We have identified forty-two lenders that predominantly originate B&C loans and we analyzed their loans separately.⁴⁰ We excluded these loans from our distribution of business comparisons because the GSEs do not purchase these loans.⁴¹ However, we included these loans in our market share estimates in order to accurately measure the GSEs' role in the affordable lending market.

Below-investment grade loans are mainly originated for borrowers that, relative to borrowers qualified under traditional conventional market underwriting criteria, have different types of income used to qualify an applicant for a loan, checkered credit histories, and limited or non-traditional uses of credit.⁴² Low-income and minority borrowers have proportionately more of these problems than white and high-income borrowers and are more likely to benefit from the more flexible underwriting of B&C lenders.

FHA also has more flexible underwriting criteria than the conventional conforming market. The characteristics of B&C loans resemble the characteristics of FHA loans. As shown in Table 2, 18.7 percent of B&C loans in 1995 were originated for borrowers with very low incomes, compared to 18.2 percent of loans for FHA borrowers. African Americans accounted

⁴⁰ We have identified B&C lenders through industry periodicals like *National Mortgage News*, *Secondary Marketing Executive*, and *Inside Mortgage Finance*. For example, The Money Store, Ford Consumer Finance, Champion Mortgage, and TransAmerica Financial Services are predominantly B&C lenders. Many of the lenders that originate manufactured housing loans also originate B&C loans. We do not include the originations of these lenders in our B&C analysis. Other traditional lenders like Countrywide and GE Capital have also begun to originate B&C loans as their lending volumes in traditional markets decline but we are unable to separate these loans from their prime loans.

⁴¹ According to HMDA data, the GSEs purchase very few loans originated by the lenders that we have identified as B&C lenders.

⁴² For example, many first-time homebuyers do not have credit histories and many minorities rely on finance companies for loans.

for 16.0 percent of all B&C loans compared to 15.3 percent of FHA-insured loans for FHA borrowers.

APPENDIX B

DATA FOR CONFORMING CONVENTIONAL MARKET

Tables 2-4 in the text limit the conforming conventional market to only FHA-eligible loans. This appendix expands that definition to include all conforming conventional loans, thus adding loans that are above the local FHA-limits but are below the national conforming loan limit, which was \$203,150 in 1995. Inclusion of these larger loans provides a complete picture of the home loan purchase activity of the GSEs.

The effects on the "distribution of business" percentages of adding the larger loans can be seen by comparing Table 2 with Table B.1. First, the affordable percentages for FHA are not affected by these changes since all FHA loans were included earlier because they are, of course, "FHA-eligible". Second, the affordable percentages for the GSEs, depositories, and conforming market are all reduced because the added loans for these sectors are much less likely to be loans for lower income families and members of minority groups than are the FHA-eligible loans for these sectors. For example, 8.2 percent of all home loans purchased by the GSEs in 1995 were for very-low-income (VLI) borrowers, compared with 12.4 of the FHA-eligible home loans that they purchased. Including the additional loans lowered the very-low-income percentage for banks slightly more than it did that for the GSEs. VLI borrowers accounted for 14.0 percent of all loans originated and held by banks, compared with 19.0 percent of all FHA-eligible loans originated and held by banks. However, for the most part, adding the larger loans does not change any of the earlier conclusions concerning the GSEs' distribution of business to disadvantaged groups, the improvement in the GSEs' purchases of affordable loans since 1992 (compare Tables 3 and B.2), and the substantial differences in performance between Fannie Mae and Freddie Mac.

Table B.3 reports market shares for FHA and the GSEs, comparable to those reported in Table 4. In this case, the market includes all home purchase loans in metropolitan areas except jumbo loans above the conforming loan limit of \$203,150. Specifically, the market is defined as (1) FHA loans, (2) loans guaranteed by the Veterans Administration (VA), and (3) loans originated in the conforming conventional market, including mobile home and B&C loans. In Tables B.1 and B.2, the "conforming market" figures included (3), but without mobile home and B&C loans, as discussed in Appendix A.

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