

Changes in Foreign National Lending: How will it impact your future business?

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Changes in lending availability for foreign nationals here in the U.S. have been cathartic. The general trend is back towards a more centralized loan origination and delivery system.

What this means is that fewer options will remain for our foreign national clients. So we can all be better prepared to meet the challenging environment of our real estate industry, let's examine some of those changes.

We will start with Changes in Secondary Market, characterized by Wall Street. Then we'll examine how changes at the Wall Street level have trickled down into the Institutional Levels. From there, we'll talk about how the institutions themselves have made fundamental changes in their Loan Products. We shall review four key aspects of foreign national lending programs: Down Payments, Rates, Lender Fees and how all of these can impact Time Frames to Close.

Changes In Secondary Market have been well publicized in many public forums. Wall Street has lost the ability to take packages of loans from many institutional lenders (bundle or re-package them into a pool and sell the pool off to an investor). We refer to these types of pools of mortgages as collateralized debt obligation (C.D.O.) or collateralized mortgage obligation (C.M.O.).

The plight of Bear Stearns is a key example. With the market for pooled mortgage sales shutdown on Wall Street - the only other source of secondary liquidity for primary institutional lenders (the wholesalers to whom mortgage brokers turn for clients) are the GSE's - Fannie Mae and Freddie Mac.

However, loans to Foreign Nationals by originators and banks may no longer be eligible for sale/purchase by the GSE's. So where does that leave the foreign national purchaser? Loans to Foreign Nationals will come from a reduced number of specialized Portfolio or Pocket Institutional Lenders for the near future.

Changes at the Institutional Level will manifest themselves in the reduced number of lenders mentioned above. Institutional Fallout from the lending industry has also been well publicized. Wachovia, Sun Trust, Chase, Bank Atlantic and Bank United (as of Sept. 5, 2008), all former industry leaders in products for foreign nationals. All of these institutions are now out of the lending business for foreign nationals.

Only a few specialized institutions will accept the risk associated with lending to a foreign national. These are companies who will originate and hold and service that loan over the term of the loan. Because the institution holds the loan in its own 'pocket' or 'portfolio' they garner the term "pocket lender."

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Portfolio - Pocket Lenders is the way it'll be for the near future - at least insofar as the secondary market remains a broken mechanism. Since those options will center on what we call 'pocket' or portfolio lenders, who originate and hold those loans within their own portfolios, only a few institutions remain for the Canadian borrower. TD Commerce Bank, RBC and Harris Bank (a unit of Bank of Montreal) are three examples. TD Commerce Bank is new to Canadian

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Lending in Florida, so their portfolio is being grown; however, the converse is the case at RBC.

The RBC portfolio experienced its greatest growth during the 'boom' years of 2004-2006. Consequently, loans originated during that time frame are over valued relative to the new real estate values in Florida. As a result their portfolio was being contracted and constrained by RBC's management in the face of increasing reserves for loan losses. Remember these firms no longer have access to the secondary market for the repurchase of these loans in the form of CDO/CMO issuances. Consequently they can and have, adjusted the amount of risk they're prepared to assume.

Contraction in lending risk has been seen in the down payments, which is one of the most 'up-front' methods of reducing loan exposure. Down payments



have been increased to 30 percent in most cases and can be as high as 45 percent conditioned on property use and whether it's located in a declining market county (includes all counties in southern half of Florida). And now, a word about down payment seasoning.

The down payments (in toto) must be brought to the U.S. and left in a domestic bank for 30 days, where borrowing is to be used. This rule has become more stringently enforced than ever. The sourcing and seasoning of down payment monies is primarily influenced by Anti-Money Laundering regulations and the Patriot Act legislation. This means that a Canadian or other foreign national looking to buy U.S. real estate must move their down payment funds plus closing costs to the U.S. a full 30+ days before even going under contract. A typical contract period is 30 days; thus, foreign nationals would potentially be looking at a time to purchase period of 60 or more days.

Rates, however are not typically locked for 60-day periods. But one of the other changes in loan programs has been rate adjustments. As risk increases, so do rates; generally between .75 percent and 1.25 percent (conditionally). It is also a given economic theorem that rates also will experience further increases as the number of available loan products decreases. Basic economics - the fewer sellers in a given market for a good or service, they can charge whatever the market will bear (or whatever the public will pay). Moreover the whole monthly cost of the debt service will change for the foreign national borrower. Especially since escrow accounts are now mandatory for taxes and/or insurance, mandated in some rule changes adopted by the Treasury Department under the HOEPA statutes (July 15, 2008). But depending on the lenders appetite for the risk, a few buy-out programs remain, however at no small cost to the borrower.

Changes in Loan Programs have very prominently manifested themselves in lender fees charged to foreign

national borrowers. Lender Fees have increased relative to the markets contraction. Its analogous to the Airline Syndrome: where the pressing need from the lenders (or airlines) perspective is to raise revenues as much as possible. The need for additional income is especially pressing for the purposes of either increasing reserves for loan losses, or raising capital such as through a stock buy-back.

Here's an example of the lenders fees charged to a recent client from Canada. A 7/1 LIBOR ARM (5/2/5) 30 year term, 3 year soft pre-pay. The rate was 7.375 percent. The Lender Fee was 1.25 percent of the loan amount, plus an additional \$700 in lender under-writing fees. Now some of my Realtor partners have asked me, "Why can't I just steer my purchaser into a portfolio lender directly?" However be warned, portfolio lenders are charging 1 to 2 points as origination fee or in total fees to recoup these revenues for reasons similar to those stated previously.

So, rates are going up and fees are going up as is the amount of time that the down payments must be here seasoning in a Florida banking institution. All of this directly impacts the time frames to close a real estate purchase for a foreign national where financing is to be involved. Underwriting of borrower income and assets is more heavily scrutinized than ever! Sourcing and seasoning adds 30+ days to the loan under writing period unless you and your client are prepared for this from the beginning.

Foreign National Lending is now - more than ever before - a 'niche' specialty. In order to make the process of foreign national client intake as smooth as possible, know who your foreign national lending specialist is and involve them as early in process as possible.

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