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Debt & Equity Journal: Fannie Mae Streamlines Underwriting as Credit Crunch Eases

By Erika Morphy

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Washington, DC—Fannie Mae recently introduced new regulations designed to reduce waiver requests from lenders. In essence, it transferred many of the decisions it formerly made in underwriting transactions to DUS lenders.

The new regs, says Colin Whittier, vice president of KeyBank Real Estate Capital in Dallas, “will allow us to quote a lot more deals in a shorter period of time.” Whittier says Fannie and Freddie Mac looked at deals in 2006 and the first half of 2007 on a case-by-case basis. “Lenders would have to come to them and say, ‘I want to win this deal and XYZ conduit is quoting it this way. I need to match it.’ Fannie would most likely agree, or, occasionally, not,” he explains.

The new standards touch upon size of deal, IO loans and new designations for LTV ratios and debt service coverage. To give one example: a mortgage with a loan term between seven to 10 years and an LTV equal to 70% or lower can be underwritten with a full term IO period without special approval.

Ironically, the new regulations were developed in part to help Fannie and its DUS lenders compete more effectively against the once ultra-competitive conduit market. Now, of course, the conduit market is frozen, although there are signs it is beginning to thaw.

General pricing has come in five to 10 basis points over the last two weeks for all assets, Whittier reports. On standard fully leveraged transactions, the GSAs were quoting 145 to 150 over the 10-year Treasury. Now 135 to 145 is the current pricing, he says.

In addition, in general, conduit pricing from a break-even perspective has improved: When the CMBS market imploded in late July and August, break even was 200 basis points over range. “Now we are seeing break even in the 165 to 175 range," Whittier says. "And my understanding is life insurance companies are just inside of where the conduits are.”

Other more subjective signs include a return on the part of the GSAs to "historical norms" in underwriting, says Christopher Finlay, co-founder and managing principal of Mission Residential, a Vienna, VA-based real estate investment firm that owns and operates apartment complexes in the Sunbelt states.

“It is all relative, of course. There was a lot of credit loosening during the hey day of the capital markets. When the credit crunch occurred in mid August, there was a real pull back. Nobody was clear as to what was going on so the immediate response was to retreat.” Fannie was part of that retreat, Finlay says. “Now it seems as though it is loosening--at least

compared to where it was a month ago--but still more conservative than the beginning of the year," he adds.

For instance, a year ago it was common to see a 10% debt service coverage ratio. Now coverages are returning to 15% to 20%, Finlay reports.

But while no one expects to see the capital markets return to 2005-2006 standards, Fannie's new underwriting standards should help bolster multifamily trades as the markets slowly improve. It delivers a much more streamlined process and less cumbersome documentation requirements, says Ted Patch, senior vice president and chief production officer at Bethesda, MD-based Green Park Financial, one of the largest dedicated multifamily lenders.

"Overall, it is a much more efficient execution for them," he says. "It gives us the ability to do what we think we do best--which is structure complicated deals in creative ways that effectively meet the borrowers' needs."

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