CMG MI Signals
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After the Bailout

Realigning the Mortgage Industry through Performance Pricing

By Brian Shepherd, Senior Vice President and General Manager, CMG Mortgage Insurance Company

The current economic turbulence can be traced to the weakness of the housing markets, a weakness long masked by the real estate boom that continued from 2003 to early 2007 — itself created by an oversupply of cheap money. Analysts, government regulators, lenders and the press are all realizing now that too many loans during those years were originated without due regard to the borrower's ability to repay the loan. In many cases, borrowers may have been matched with loans inappropriate to their circumstances but lender approvals were rationalized by the assumption that rising collateral values would provide an escape route.

As seasoned Credit Union mortgage lenders understand, the criteria for loan approval, even in Credit Unions, were liberalized in recent years. Even so, owing to their more conservative lending practices and the higher credit quality of their membership, Credit Unions have been impacted by the current crisis much less than banks.

However, Credit Union prime borrowers live in the same declining neighborhoods as subprime borrowers. Because of this, members have lost the equity cushion that previously allowed the options of refinance or property sale to solve financial life-events. The first line of defense against a foreclosure is normally the borrower's equity: No equity = no defense. More borrowers are defaulting because they are losing equity instead of building it.

Adapting to the Environment is Essential

The frequency of defaults for mortgage-insured Credit Union loans is increasing beyond recent trends generally — and especially among members with low FICO® scores. Severity has also begun to increase as proceeds from foreclosure sales decline. We are seeing the beginning of a long-term up-shift in mortgage default risk, which will continue even in the "better days ahead" of flat home values.

Brian Shepherd, AMP, is Senior Vice President and General Manager of CMG Mortgage Insurance Company (CMG MI), which exclusively serves credit unions. With two decades of experience in the credit union and mortgage insurance industries, Mr. Shepherd is familiar with the challenges of managing a mortgage lending business in a wide range of economic circumstances.

In 2006 and 2007, in response to the industry-wide introduction of high-risk mortgages, we introduced FICO-based pricing for A-Minus and 100% LTV loans — pricing that takes into account the predicted performance of loans based on the FICO scores of members. Credit Unions have already utilized this "performance-based pricing" in their own consumer lending programs for many years. As CMG Mortgage Insurance Company (CMG MI) examines the present and future lending environment, we believe it is more appropriate to expand our performance-based pricing to **all** LTV categories eligible for mortgage insurance.

Performance-based pricing will allow CMG MI to continue supporting a range of higher-risk mortgage insurance products and enable Credit Unions to continue to offer members mortgage insurance rates lower than those available at banks and other financial institutions. Details of CMG MI's new pricing by FICO/LTV ranges will be available on October 27 and will become effective beginning December 15, pending state approvals.

In the current environment, CMG MI remains a strong and effective mortgage insurance provider to Credit Unions, with insurer financial strength ratings most recently affirmed by Standard & Poor's (AA-) and Fitch Ratings (AA). (The rating agency reports can be found on our Website at **www.cmgmi.com/whatsnew**.) CMG MI was profitable during the first half of 2008 and as such, added earnings to capital. While mortgage insurance claim filings are higher than in previous years, we are well able to meet our commitments and support our Credit Union customers.

At CMG MI, we are committed to maintaining our insurer financial strength into the long-term future by offering products to Credit Union lenders that support sustainable homeownership for Credit Union members. To do this, our premiums and the performance attributes we measure need to be appropriate to Credit Union member performance and the housing economy in which mortgages will be originated.

CMG Mortgage Insurance Company
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