CMG MI Signals

Summer 2009

Capital Concerns

CMG MI Takes Action Now to Support Credit Unions Long-Term

By Joe Dillon, CPCU — Senior Vice President and General Manager, CMG Mortgage Insurance Company

The recession continues to impact lives and businesses across the United States and abroad but, for Credit Unions that offer mortgage lending, it has been a mixed experience. While many are confronting the problem of delinquent loans and foreclosures for the first time, Credit Unions have also benefited as overextended banks have been forced to retreat from the mortgage marketplace. In today's environment, Americans perceive Credit Unions to be more trustworthy and solvent financial advisers than other lending institutions – a view endorsed by the U.S. Congress, which has declared the Credit Union industry blameless for the housing debacle.

The result is that many Credit Unions are seeing a boom in the number of mortgage applications they receive. The Credit Union share of the mortgage industry has doubled since the crisis began, reaching above 5%. In the words of Bob Dorsa, President of the American Credit Union Mortgage Association, "This is a time of real opportunity for Credit Unions. The personalized service and community-based orientation that they bring to the housing market have real resonance for Americans who are realizing that getting into the home is not the only issue – it's being able to stay there for the long term. Credit Unions make every effort to work with their members when they run into difficulties."

Many members now applying for home loans have excellent credit and other risk characteristics that in normal times would make them ideal candidates for home-ownership, despite the lack of a 20% down payment. However, Credit Unions have discovered that just as the boom has materialized, private mortgage insurers are issuing more restrictive guidelines that limit eligibility – and they want to know why.

Joe Dillon is Senior Vice President and General Manager at CMG Mortgage Insurance Company (CMG MI), which exclusively serves Credit Unions. Mr. Dillon came to CMG MI in 2009 from CUNA Mutual Group, where he served as Products Executive and managed the financial aspects of the Bond Program, Special Insurance Package, Collateral Protection and Property & Liability. With nearly four decades of experience in the insurance industry, Mr. Dillon holds designations as a Chartered Property Casualty Underwriter (CPCU), Associate in Risk Management (ARM), Associate in Fidelity-Surety Bonding (AFSB), Associate in Underwriting (AIU) and Associate in Reinsurance (ARE).

Looking at the Larger Picture

CMG Mortgage Insurance Company (CMG MI) continues to be the highest-rated mortgage insurer in the industry – meaning that the rating agencies have extensively analyzed our financial strength and can confirm our company as the most reliable insurance counterparty in the industry for the Credit Unions we work with. Maintaining that rating, and by extension our ability to continue to support the needs of our customers, demands that CMG MI implement key strategic measures to allow us to preserve capital while continuing to pay claims and facilitate loss mitigation measures that help keep families in homes.

The state and federal regulations governing mortgage insurance require that once an MI company insures a loan, it must immediately be able to support the risk the policy represents through the capital it keeps in reserve for that purpose. However, the premium paid for the mortgage insurance by the lender is seldom available up-front; more usually it is pro-rated on an annual or monthly basis and is attached to the borrower's mortgage payments. Furthermore, when considering the average premium associated with a policy in comparison to the risk that policy represents, it's clear that the cost of a single claim can easily outweigh the combined premiums of dozens of policies. A mortgage insurer is required by law to set aside contingency reserves – half of all premium dollars earned – into a trust account for ten years. For those ten years, contingency reserves can only be accessed during severe credit events. Because MIs are required to have these reserves, they are well positioned to continue doing business even in turbulent market conditions.

Just as many Credit Unions must limit the number of loans they make because of constraints imposed by their Loan-to-Share Ratio, private mortgage insurers (MIs) must limit the number of loans they insure because of their Risk-to-Capital ratio. The Risk-to-Capital ratio, like a golf score, improves as it declines in value and is calculated as the total risk of policies in force divided by the capital available to service the risk. What causes the ratio to rise? Actions that increase exposure (such as the writing of new insurance) and results that diminish capital (for example, losses resulting from new delinquencies) work adversely against the ratio.

Under normal conditions, MIs are able to accommodate most of their customers' requests for mortgage insurance because the number of claims is relatively small. However, due to the current recession, all mortgage insurers – as well as the lenders they serve – are coping with an unprecedented number of mortgage delinquencies and foreclosures.

At their most basic, MIs were set up to pay claims and today they are meeting their obligations. During the last two and a half years, the private mortgage insurance industry has paid to Fannie Mae, Freddie Mac and other investors more than $15 billion in loss settlements.

At the same time, MIs are actively assisting their customers to mitigate the losses on the loans they insure, with the larger goal of keeping families that are under stress in their homes. Like our Credit Union customers, CMG MI understands the value of homeownership to the larger community as well as to the family involved and that averting the misfortune of foreclosure is well worth the money spent. Loss mitigation is expensive but it is an effort that reaps rewards over the long term. Because of its loss mitigation efforts, through May 2009, CMG MI has helped prevent 263 foreclosures and helped Credit Unions keep 577 member families in their homes.

The bottom line is that CMG MI, instead of being able to focus almost exclusively on insuring loans, must direct a large share of resources and our reserve capital to support claims and loss mitigation efforts. Not to do so would be to betray our customers' trust. On the other hand, to continue to insure loans at the same level as in the past would deplete our capital reserves and jeopardize our financial rating – which is the key reason why Credit Unions continue to entrust their business to CMG MI. Because of our rating, you have the confidence that we will be there in the future to pay your claims and mitigate your losses on the loans we insure.

Preparing for the Long Term

CMG MI is in an excellent financial position relative to other MI companies, thanks to the high quality of Credit Union mortgage loans and our own strategic business decisions, as recognized by the rating agencies.

The capital preservation efforts we continue to implement this year will enable us to emerge along with our Credit Union customers into a post-recession economy with greatly enhanced financial capabilities and capacity, ready to provide credit enhancement on new originations to meet the anticipated demand of a revived housing market.

Our actions now are key to achieving that future scenario. By successfully managing our risk-to-capital ratio now through a prudent approach to risk management, CMG MI will be able to continue to serve our customers over the long term. As we move into 2010 and 2011, Credit Unions will be able to continue to count on CMG MI for their mortgage insurance needs, while appreciating the guidance and support we have been able to provide during one of the worst financial crises in American history.

The current market will not last forever. We understand that you have been frustrated by the actions of the MI companies as they pursue capital preservation strategies and introduce stricter guidelines to reduce their risk exposure. Some of you may be asking, What is the use of private mortgage insurance at all? Why not utilize FHA mortgage insurance instead?

CMG Mortgage Insurance Company (CMG MI) supports sustainable homeownership with products and services that can help Credit Unions keep members in their homes. What are the challenges to homeownership in your community – and how can we help? Let us know what you think and what we can do for you by contacting your CMG MI Account Executive or sending an e-mail to CMGMortgage.InsuranceCo@cmgmi.com.

CMG MI understands your point of view. However, we believe that the restructured housing market that will emerge from the present confusing situation will be one in which private mortgage insurers will be recognized as a valuable – even essential – component. The leading role we have taken during this crisis has helped prevent much of the worst from happening. By continuing to pay claims, prevent foreclosures, and train lenders and Credit Unions in how to manage risk and conduct loss mitigation, the MI companies have proven their value.

The role of the FHA is an important one. However, it is the existence of the private mortgage insurance industry that has allowed the FHA in the past to operate responsibly without accumulating an overwhelming amount of risk. Historically, mortgage insurance companies have insured between 10 to 16 percent of the new originations market. Without private mortgage insurance, the FHA – and by extension the American taxpayers, who are already shouldering the brunt of the overall economic bailout – would have to assume even greater levels of risk at a time when its capital adequacy is declining. Given the fact that the FHA will be burdened with a higher risk-in-force due to a larger market share and significantly higher loan limits, such a course is simply unfeasible.

In any recession, the temptation is to focus on short-term gains. Companies that adopt this strategy often sacrifice their financial health and long-term survival. CMG MI recognizes the responsibility we have to Credit Unions to be here after the recession is past. Our strategy is to serve you, in both boom times and bad times, by taking appropriate business decisions that look beyond current economic challenges.

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