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New Program for Buyers, With No Money Down

By JOHN LELAND

MILWAUKEE — When the housing bubble burst, one of the culprits, economists agreed, was exotic mortgages, including those that required little or no money down.

But on a recent evening, Matthew and Hannah Middlebrooke stood in their new $115,000 three-bedroom ranch house here, which Mr. Middlebrooke bought in June with just $1,000 down.

Because he also received a grant to cover closing costs and insurance, the check he wrote at the closing was for 67 cents.

“I thought I’d be stuck renting for years,” said Mr. Middlebrooke, 26, who earns $32,000 a year as a producer for a Christian television ministry.

Although home foreclosures are again expected to top two million this year, Fannie Mae, the lending giant that required a government takeover, is creeping back into the market for mortgages with no down payment.

Mr. Middlebrooke’s mortgage came from a new program called Affordable Advantage, available to first-time home buyers in four states and created in conjunction with the states’ housing finance agencies. The program is expected to stay small, said Janis Smith, a spokeswoman for Fannie Mae.

Some experts are concerned about the revival of such mortgages.

“Loans that have zero down payment perform worse than loans with down payments,” said Mathew Scire, a director of the Government Accountability Office’s financial markets and community investment team. “And loans with down payment assistance” — like Mr. Middlebrooke’s — “perform worse than those that do not.”

But the surprise is the support these loans have received, even from critics of exotic mortgages, who say low down payments themselves were not the problem, except when combined with other risk factors like adjustable rates or lax underwriting.

Moreover, they say, the housing market needs such nontraditional lending, as long as it is done prudently.

“This is subprime lending done right,” said John Taylor, president of the National Community Reinvestment Coalition, an umbrella group for 600 community organizations, and a staunch critic of the lending industry. “If they had done subprime this way in the first place, we wouldn’t have these problems.”

At Harvard’s Joint Center for Housing Studies, Eric Belsky, the director, said the loans might be the type of step necessary to restart the housing market, because down payment requirements are keeping first-time home buyers out.

“If you look at where the market may get strength from, it may very well be from first-time buyers,” he said. “And a very significant constraint to first-time buyers is the wealth constraint.”

The loans are the idea of state housing finance agencies, or H.F.A.’s, quasi-government entities created to help moderate-income people buy their first homes.

Throughout the foreclosure crisis, the state agencies continued to make loans with low down payments, often to borrowers with tarnished credit, with much lower default rates than comparable mortgages from commercial lenders or the Federal Housing Administration. The reason: the agencies did not offer adjustable rates, and they continued to document buyers’ income and assets, which many commercial lenders did not do. In 2009, the agencies’ sources of revenue dried up, and they had to curtail most lending.

Then they created Affordable Advantage. The loans are 30-year fixed mortgages, with mandatory homeownership counseling, available to people with credit scores of 680 and above (720 in Massachusetts). The buyers have to put in $1,000 and must live in the homes.

All of these requirements ease the risk, said William Fitzpatrick, vice president and senior credit officer of Moody’s Investors Service. “These aren’t the loans that led us into the mortgage crisis,” he said.

So far Idaho, Massachusetts, Minnesota and Wisconsin are offering the loans. The Wisconsin Housing and Economic Development Authority has issued 500 loans since March, making it the first state to act. After six months, there are no delinquencies so far, said Kate Venne, a

spokeswoman for the agency.

The agencies buy the loans from lenders, then sell them as securities to Fannie Mae. Because the government now owns 80 percent of Fannie Mae, taxpayers are on the hook if the loans go bad.

The state agencies oversee the servicing of the loans and work with buyers if they fall behind — a mitigating factor, said Mr. Fitzpatrick of Moody's.

"They have a mission to put people in homes and keep them in homes," not to foreclose unless other options are exhausted, he said. The loans have interest rates about one-half of a percentage point above comparable loans that require down payments.

Ms. Smith, the spokeswoman for Fannie Mae, distinguished the program from loans of the boom years that "layered risk on top of risk."

With the new loans, she said, "income is fully documented, monthly payments are fixed, credit score requirements are generally higher, and borrowers must be thoroughly counseled on the home-buying process and managing their mortgage debt."

For Porfiria Gonzalez and her son, Eric, the loan allowed them to move out of a rental house in a neighborhood with a high crime rate to a quiet street where her neighbors are retirees and police officers.

Ms. Gonzalez, 30, processes claims in the foreclosure unit at Wells Fargo Home Mortgage; she has seen the many ways a mortgage holder can fail.

On a recent afternoon in her three-bedroom ranch house here, Ms. Gonzalez said she did not see herself as repeating the risks of the homeowners whose claims she processed.

"I learned to stay away from ARM loans," or adjustable rate mortgages, she said. "That's the No. 1 thing. And always have some emergency money."

When she first started shopping, she looked at houses priced around $140,000. But the homeownership counselor said she should keep the purchase price closer to $100,000.

"They explained to me that I don't need a $1,200-a-month payment," she said.

The counselor worked with her real estate agent and attended her closing. On May 28, Ms. Gonzalez bought her home for $90,500, with monthly payments of $834. After moving expenses, she has kept her savings close to $5,000 to shield her from emergencies.

“If I had to make a down payment, it would have wiped out my savings,” she said. “I would have started with nothing.”

Now, she said, she is in a home she can afford in a neighborhood where her son can play in the yard. A neighbor brought her a metal pink flamingo with a welcome sign to place by her side door.

“My favorite part is the big backyard,” said Eric, 10. “And that’s pretty much it.”

“You don’t like it that it’s a quiet, safe neighborhood?” his mother asked.

“Yeah, I do.”

“He didn’t go out much with kids in the old neighborhood,” she said.

“Because they were bad kids,” he said.

Ms. Gonzalez said that owning a house was much more work than renting, and that when the basement flooded during a heavy rain, her heart sank.

“But I look at it as an investment,” she said, adding that a similar house in the neighborhood was on the market for $120,000.

Prentiss Cox, a professor at the University of Minnesota Law School who has been deeply critical of the mortgage industry, said the program met an important need and highlighted the track record of state housing agencies, which never engaged in exotic loans.

“It’s not a story people want to hear, because it won’t bring back the big profits,” Mr. Cox said. “The H.F.A.’s have shown how the problems of the last 10 years were about having sound and prudent regulation of lending, not just whether the loans were prime or subprime.”

He added, “One of the great and unsung tragedies of the whole crisis was the end of the subprime market.”