



ANNUAL REPORT TO CONGRESS FISCAL YEAR 2011 FINANCIAL STATUS FHA MUTUAL MORTGAGE INSURANCE FUND



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
NOVEMBER 15, 2011





FHA Single Family Programs in 2011



FHA Continues to Play a Vital Role in American Homeownership

In this past year FHA:

- Insured its third highest dollar volume ever, \$236 billion – \$218 billion in single family and \$18 billion in HECM – on a total of over 1.27 million loans.
- Provided access to credit for over 770,000 homebuyers – over 585,000, or 75%, of whom were first-time buyers.
- Was used by a majority of first-time and minority home buyers needing mortgage financing.
 - 56 percent of all first-time homebuyers in 2010, according to the National Association of Realtors 2010 Home Buyer Survey
 - 60 percent of all African-American and Hispanic homebuyers in 2010, according to HMDA reports



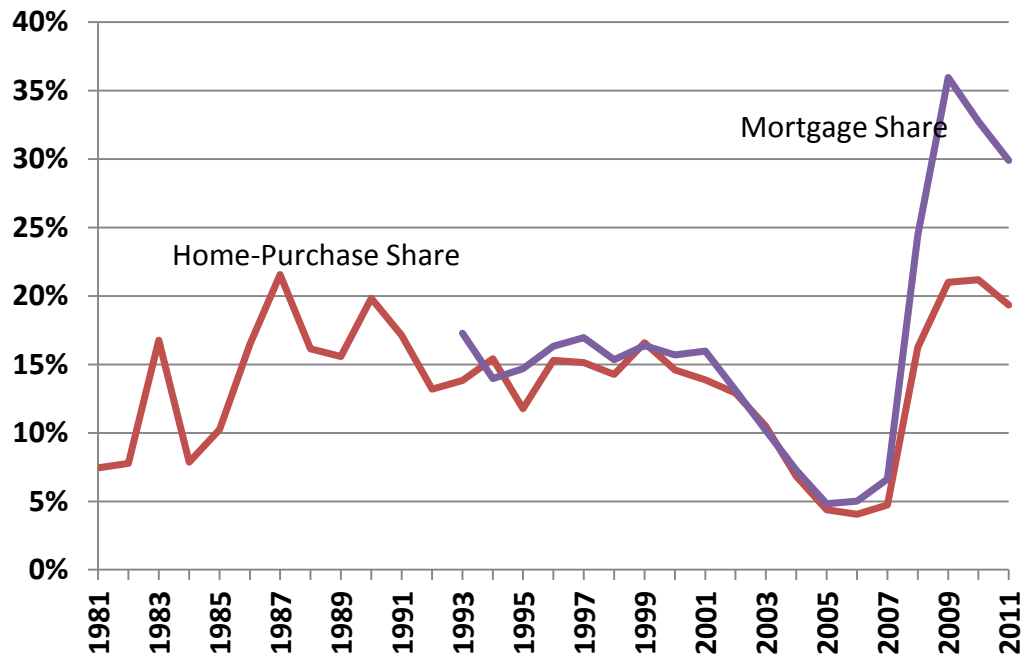
FHA Continues to Play a Vital Role in American Homeownership (contd).

- Provided refinancing for more than 440,000 homeowners seeking to take advantage of historically low interest rates, with average savings of over \$160 per month.
- Passed the historic marker of having insured 40 million single-family loans.
- Exceeded \$1 trillion in active insurance on more than 7 million loans.



FHA Market Shares Continue at Historic Levels

FHA Share of Home Purchases and Home Purchase Mortgages



Source: U.S. Department of HUD/FHA analysis of various data sources.

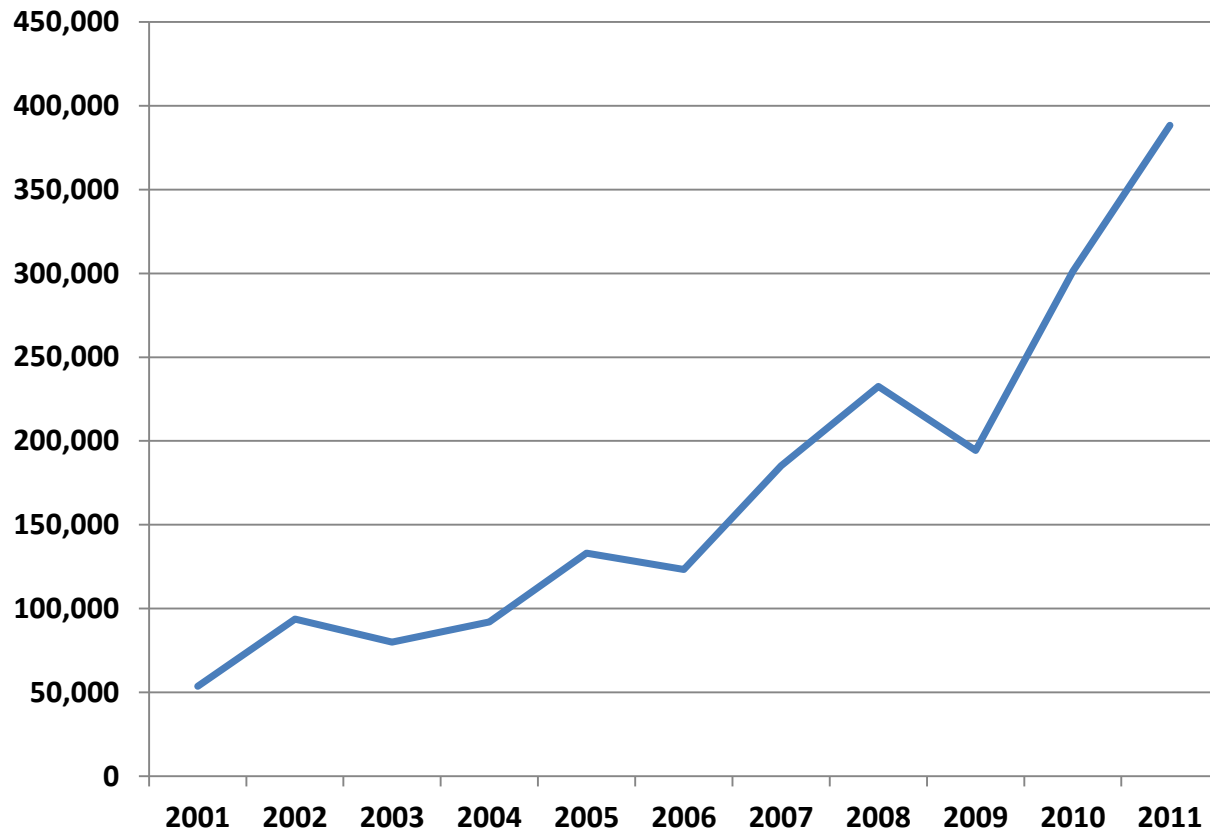


FHA is Protecting Homeownership for Households Facing Financial Difficulties

- In FY 2011, FHA loss mitigation tools were used to cure 362,000 defaults, and yielded the lowest re-default rates of the past five years.
 - At the end of FY 2011, there were an additional 155,000 open cases in which FHA servicers were working with distressed borrowers to develop loan reinstatement plans.
 - Another 26,000 avoided foreclosure via short sales.
- 142,000 distressed homeowners had their monthly payments reduced through loan modifications.
 - Traditional loan modifications reduced payments by 11 percent (\$85) on average.
 - FHA-HAMP actions reduced payments by 24 percent (\$218) on average.



FHA Again Set a Record for Number of Assisted Delinquency Reinstatements



Source: U.S. Department of HUD/FHA.



The Quality of FHA Business Continues to Improve

- The FY 2011 book of business has an expected economic value of close to \$11 billion – nearly double the actuaries’ projection for this book in last year’s report.
- Over the past three years, FHA paid out a record \$37 billion in MMI claims, while simultaneously increasing MMI Fund loss reserves by \$20 billion.
- The credit quality of FHA borrowers in FY 2011 set a new record, as the average decision credit score across all borrowers broke 700 for the first time ever.



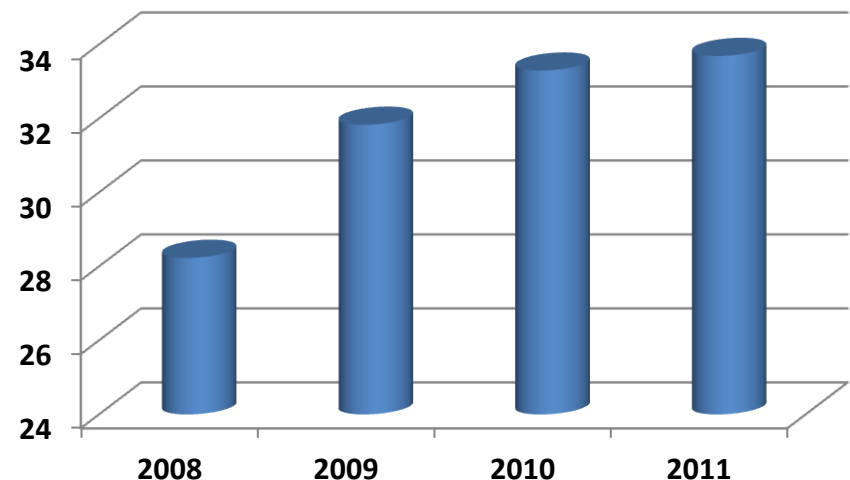
Financial Position of the MMI Fund



MMI Fund Balances are Up Slightly

- MMI Fund balances readily available to FHA total \$33.7 billion, compared with \$33.3 billion one year ago.
- Claim expenses were greater than the sum of premium revenue and property recoveries for the year. Premium revenue was down due to lower volumes of new insurance and the switch to a greater reliance upon the periodic rather than upfront premium. Over time, however, total premium receipts under the new rate schedule will be higher.

**MMI Fund Account Balances
(billions of dollars)**



Source: U.S. Department of HUD/FHA.



Report of the Independent Actuaries



The MMI Fund Remains Actuarially Sound

- The Fund has excess reserves of \$2.55 billion, yielding a capital ratio of 0.24%.
 - This is down from \$4.7 billion and 0.50% last year.
 - Total capital resources are \$33.7 billion, up \$400 million from last year
- Changes negatively affecting this year's valuation include:
 - An additional decline in national home prices by over 5 percent in the base-case forecast.
 - Increasing numbers of active loans having had previous defaults; the actuaries now include factors for their elevated redefault potential in the future.
 - A large number of loans are caught in lengthy periods of serious delinquency and foreclosure processing due to the ongoing litigation and settlement discussions regarding robo-signing and servicing concerns.
 - The actuaries assume that post-foreclosure-auction robo-signing cases will go to insurance claim, rather than be resolved in some other manner.



The MMI Fund Remains Actuarially Sound (contd).

- FHA's current underwriting and premium structure have created an actuarially sound basis for growing capital at a rapid rate once the economy and housing markets experience steady and sustained growth.
- Base-case projections show the capital ratio reaching 2% again in 2014, sooner than was projected in last year's report.
- This three-year re-capitalization projection matches FHA experience from 1991-1994

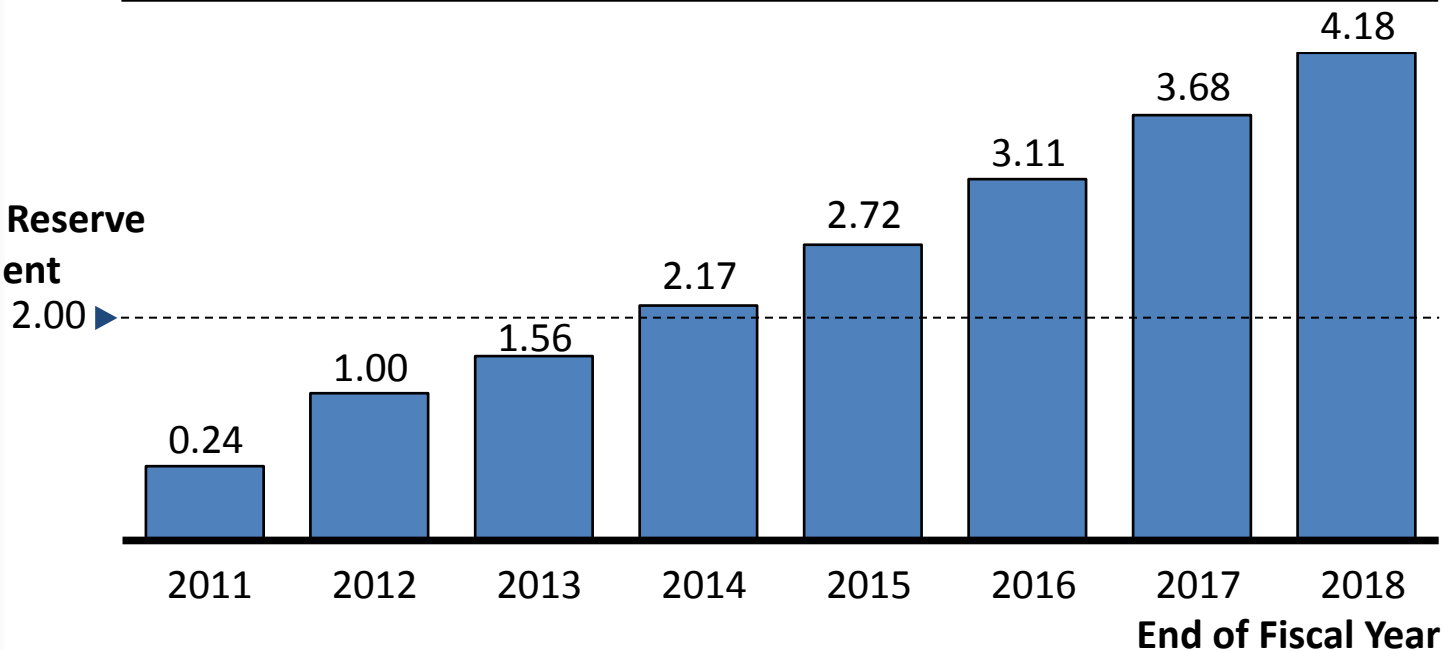


Without Additional Policy Changes to Future Business, the Capital Ratio is projected to Exceed 2% by 2014

Capital Ratio

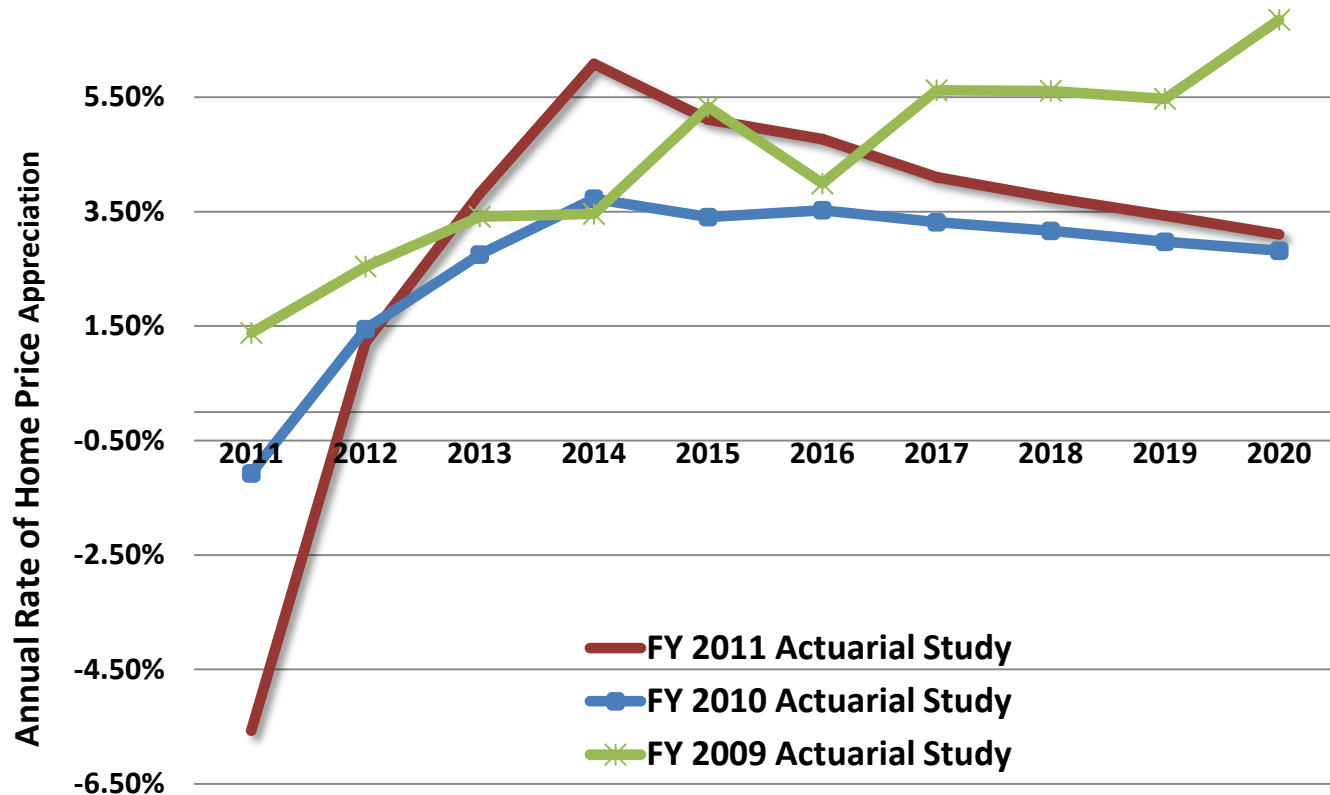
Percent

Statutory Reserve Requirement





Recent House Price Declines have Exceeded Last Year's Forecast



Source: Moody's Analytics (FY 2010 and 2011) and IHS Global Insight (FY 2009); analysis by U.S. Department of HUD/FHA; appreciation rates are across the four quarters of each fiscal year; the FY 2010 and FY 2011 series are weighted averages based upon metropolitan level forecasts and FHA insurance volumes.



The Contrast Between Old and New Business

Single-family books of business insured under this Administration are expected to be profitable, providing significant net revenues to offset losses on earlier endorsements.

Old Books

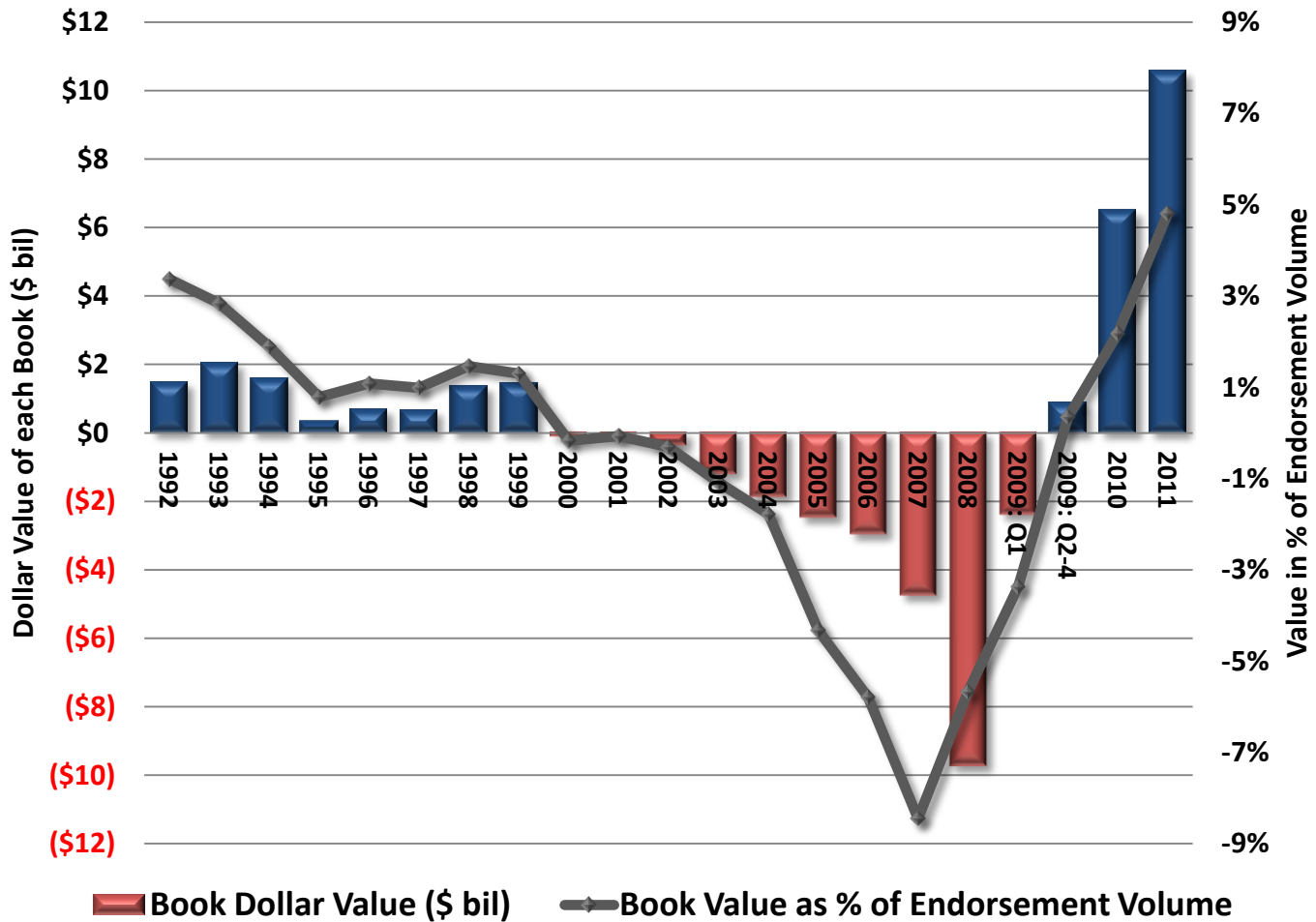
- Final losses on the 2000-2009 Q1 books are expected to exceed \$26 billion
- 2008 alone could have a net final cost of close to \$10 billion.
- The actuaries predict that claim rates on the 2006 – 2008 books could each surpass 20 percent.

New Books

- Net income generated by the 2009Q2 – 2011 books is \$18 billion.
- Borrower credit scores have increased each year, and loans having scores under 580 are virtually eliminated.
- Many borrowers have refinanced multiply times to take advantage of historically low interest rates and mortgage payments.
- Early Payment Default rates are negligible (.35% today compared to 2.23% in January of 2008).



The Economic Value of New Books of Business are Strongly Positive



Source: U.S. Department of HUD/FHA.



There Remain Downside Economic Risks

- Significant declines of home prices in FY 2012 would create a situation in which the current portfolio would require additional support.
- There is no current evidence for any widespread, sustained home price declines in FY 2012.
 - The base-case scenario provided by Moody's Analytics indicates price declines in 2011 of 5.6% and predicts a small amount of growth in prices in 2012 (1.3%), followed by more steady growth starting in 2013.
- Should the current portfolio need additional support, the first source would be the FY 2012 book, which the actuaries estimate to be worth \$9 billion.
 - The actuarial projections suggest that any further, nationwide price declines in 2012 would need to rival those of 2011 before this first level of support would be insufficient.



There Remain Downside Economic Risks (contd).

- Additionally, FHA could also implement policy changes, such as insurance premium increases, to provide additional support to the Fund.
- Only if conditions worsened substantially would the MMI Fund require any special assistance from the U.S. Treasury one year from now.
- Should the MMI Fund require special assistance from the U.S. Treasury, current law provides for there to be permanent and indefinite budget authority.
- Any special assistance would allow FHA to restore the MMI Fund capital reserve ratio to 2% in the 2016-2018 period – even under worst-case economic scenarios – and could be fully repaid within two to eight years.



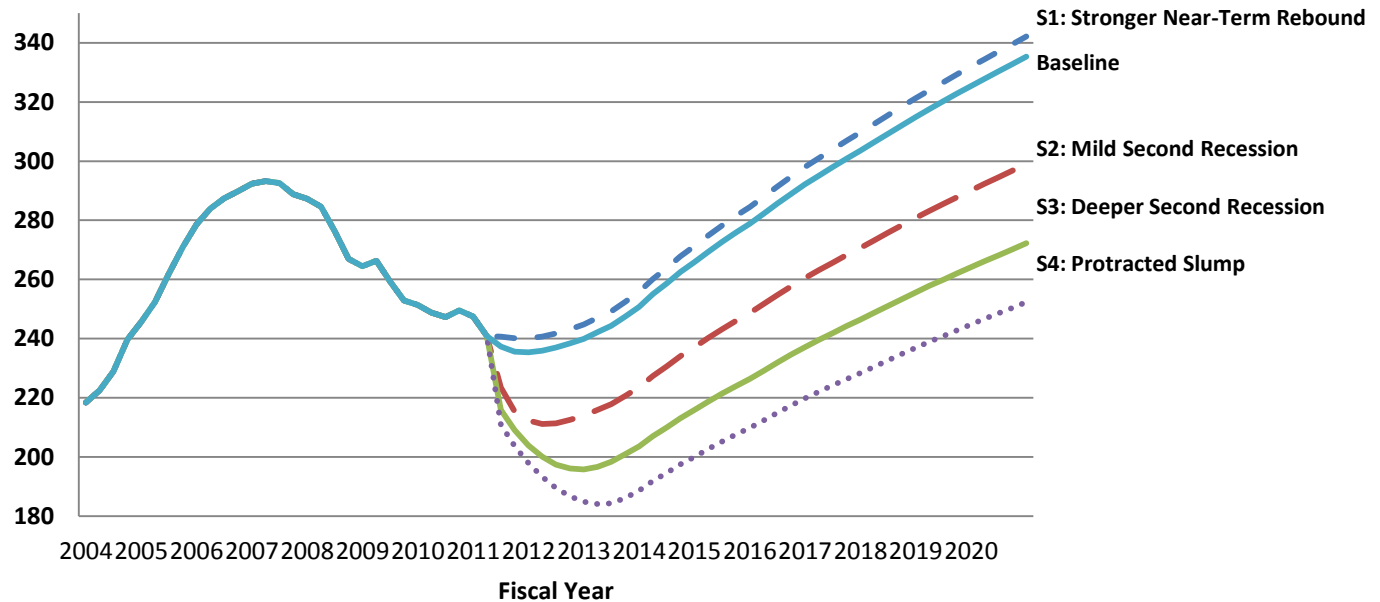
House Price Scenarios Used Represent Potentially Extreme Declines in Value

- The “Mild Second Recession” utilized by the actuaries poses an additional 9 percent decline in home prices beyond the 5.6 percent base-case decline, for a total two-year decline of 14.6 percent.
- In contrast, the worst 2-year period recorded by the FHFA was from Q2 2007 to Q2 2009, when prices fell just under 13 percent.
- Thus, even the Moody’s “Mild Second Recession” scenario is worse than the worst declines experienced since the start of the recent economic crisis.
- FHA estimates that the fund could withstand an additional decline in house prices of 4% beyond the base-case decline without experiencing a negative capital situation.



House Price Paths Used by Actuaries

FHA Portfolio Weighted House Price Indices^a



^a Portfolio weighting involved creating weighted average national price growth rates using metropolitan level forecasts and FHA active insurance volumes in **each** MSA (and non-metro areas) as of July 2011. Index values equal 100 in 1995 Q1.

Source: Analysis by the U.S. Department of HUD/FHA using historical and Moody's Analytics' forecasts of the FHFA all-transactions house price index at the metropolitan level, as adjusted by IFE Group.



FHA Continues to Take Responsible Steps to Effectively Manage its Risk

- This Administration continues to be active and vigilant in adopting policies and procedures to minimize risk exposure and accelerate the rebuilding of MMI Fund capital.
 - Premiums for both single-family and HECM programs were increased in FY2011 and both are at historic highs.
 - Significant changes have been made to the HECM program, including the development of HECM Saver and the release of guidance for lenders regarding the treatment of tax and insurance defaults
 - A comprehensive overhaul of FHA's Single Family loan review policies and procedures was undertaken, resulting in a number of changes to strengthen FHA lender monitoring.



FHA Continues to Take Responsible Steps to Effectively Manage its Risk (contd.)

- Via a forthcoming final rule, FHA will strengthen the requirements and accountability for lenders participating in the Lender Insurance Program.
- Through the Department's FHA Transformation Initiative, FHA is obtaining 21st century information technology systems to manage risk at all points of the counterparty and loan lifecycles.
- FHA is continuing to develop and implement a comprehensive risk management strategy that is integrated into all segments of FHA business and activity.