

Computers ease work in the US mortgage market

Technology is making it easier for saving institutions to process home loans and sell them to investors, as Natalie McKelvy explains

COMPUTERS are becoming more popular in mortgage processing. There are now programs that track the progress of a mortgage from the time the homebuyer applies for a loan all the way to final approval, with the analysis of the application being carried out on a computer screen. The only paper involved is the documents relating to title and the appraisal.

Over the past few years, such computerisation has enabled many savings institutions to double or even triple the volume of mortgages they can process.

An example of how an institution can computerise its mortgage processing successfully is provided by the Cenlar Federal Savings Bank in Pennington, New Jersey. The company electronically linked 11 mortgage loan origination offices in four states using computer software designed by Saddlebrook Systems of Cambridge, Massachusetts.

Cenlar is a small institution by US standards, with total assets of \$440 million, but it does a booming mortgage lending business. For the first half of 1986, the institution originated \$700 million in mortgages, compared to \$400 million for the whole of 1985.

Cenlar has 60 mortgage loan officers who take applications out in the field — in a customer's home or office, or even in his car. In the evening, the information the officers have gathered is entered into local, branch office micro-computers that feed into the institution's main computer.



The system sends summary information about the mortgage to Cenlar's underwriting department and forwards pertinent information as it is gathered. Within three days of the application, the system generates hard copy of the legally mandated forms and disclosures. As more information is added, the system generates other required forms. "When everything is complete, the system creates and prints out a standard loan application, filled out with everything but the signatures," says Andrew Young, second vice-president for management information systems at Cenlar.

When the mortgage is approved, the computer generates and prints out an acceptance letter to the applicant, including any comments or

requirements the underwriters decide to add. The computer also produces all loan closing forms and calculations.

Because Cenlar originates mortgages in several states, the processing program inserts clauses and disclaimers specifically required by a given state. The system will even produce forms required by local and federal governments. In addition to processing loans, the system can sort the loans already made enabling Cenlar to package them for investors.

Initial costs to set up the system were \$250,000, not counting employee time and the ongoing cost of subscribing to Saddlebrook's support system. The total cost to implement the system was almost \$1 million.

Young is so enthusiastic about the system that he is planning to equip mortgage loan officers with portable, lap-top computers. Officers will then be able to take applications directly by computer, shipping the information to their branch offices by modems.

Secondary mortgage market

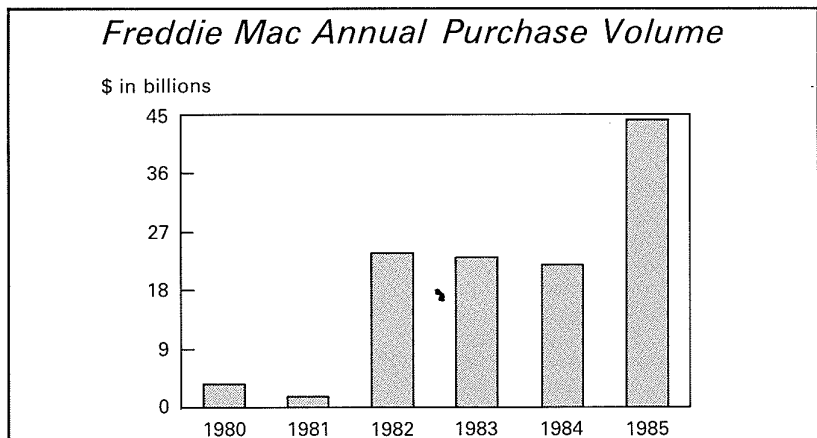
The US has a gigantic and growing investment market for residential mortgages, known as the secondary mortgage market. Many financial institutions sell anywhere from 50 to 90% of the mortgages they originate in the secondary market.

The biggest buyers of residential mortgages are an agency of the federal government — the Federal

Home Loan Mortgage Corporation, or Freddie Mac — and a quasi-governmental agency — the Federal National Mortgage Association, or Fannie Mae. Both have their headquarters in Washington, DC. A third agency, the Government National Mortgage Association, or Ginnie Mae, is part of the US government and packages mortgages insured or guaranteed by the federal government.

Fannie and Freddie buy the bulk of non-government, residential mortgages sold by mortgage originators. The two agencies then issue securities, backed by the mortgages. The securities can be backed by the agency's own name and credit or merely be packages of mortgages. In either case, the agency guarantees the payment of interest and principal to the buyer of the security.

These securities are known as a group as mortgage-backed securities, although those that are packages of mortgages, without an agency credit behind them, are known as mortgage passthroughs. These have no fixed payment schedule. The agency serves merely as a conduit, passing the interest and principal cash flows of the mortgages directly to the investor.



Buyers of mortgage-backed securities include institutional investors like pension funds and insurance companies, individual investors, and savings or financial institutions that wish to hold residential mortgages in their portfolios.

By buying and packaging residential mortgages, Fannie Mae and Freddie Mac pour capital back into the hands of mortgage originators. The originators, in turn, can then use the proceeds of their mortgage sales to make even more mortgages.

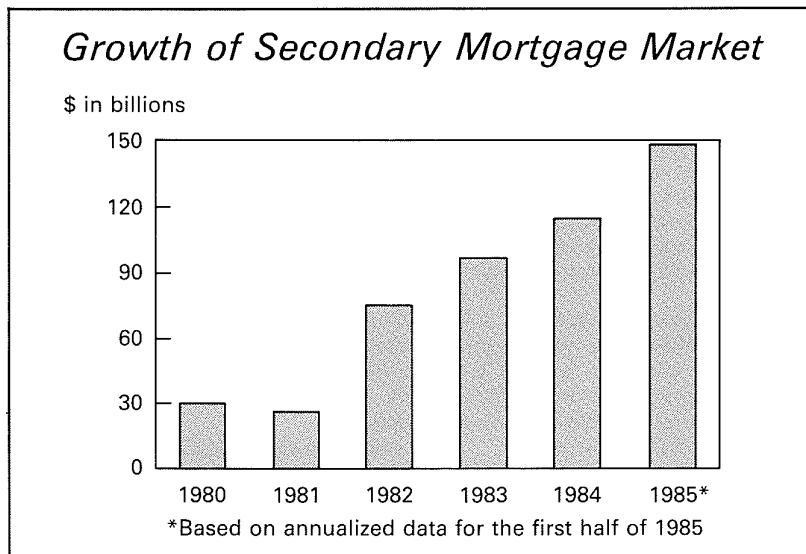
By issuing mortgage-backed securities, these two agencies are said to

have "securitised" the mortgage market in the US. They have become involved in an incredible and growing volume in mortgages, thanks to falling interest rates and the growing reluctance of savings institutions to hold mortgages in portfolio. In 1985, Freddie Mac purchased \$44 billion in residential mortgages and sold \$42 billion of mortgage-backed securities. The agency should double these numbers for 1986. For the first half of 1986, Fannie Mae issued \$23 billion in securities, compared to a volume of \$24 billion for all of last year.

The greatest progress in the use of electronics in the American mortgage market has occurred in the transactions between mortgage originators and these two, giant, mortgage agencies. Driven by the need to manage ever-increasing volumes of loans, both agencies have been gradually automating their purchase and accounting systems over the past few years. "Our volume has become so great that we never could have handled it if the loans were coming in on pieces of paper," says William Jenkins, director of mortgage information marketing for Freddie Mac.

MIDANET and MORNET

In May 1983, Freddie Mac introduced the MIDANET system which enabled sellers to deliver loans and monthly reports to the agency on



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magnetic computer tape or through a direct computer link. It eliminated the need to fill in paper forms for every mortgage sold to the agency.

The original MIDANET system was economical only for originators with a large volume of loans to sell. However, earlier this year, the agency introduced a new version of the program that works on personal computers. It can be used by smaller institutions with only small volumes of loans to sell to the agency.

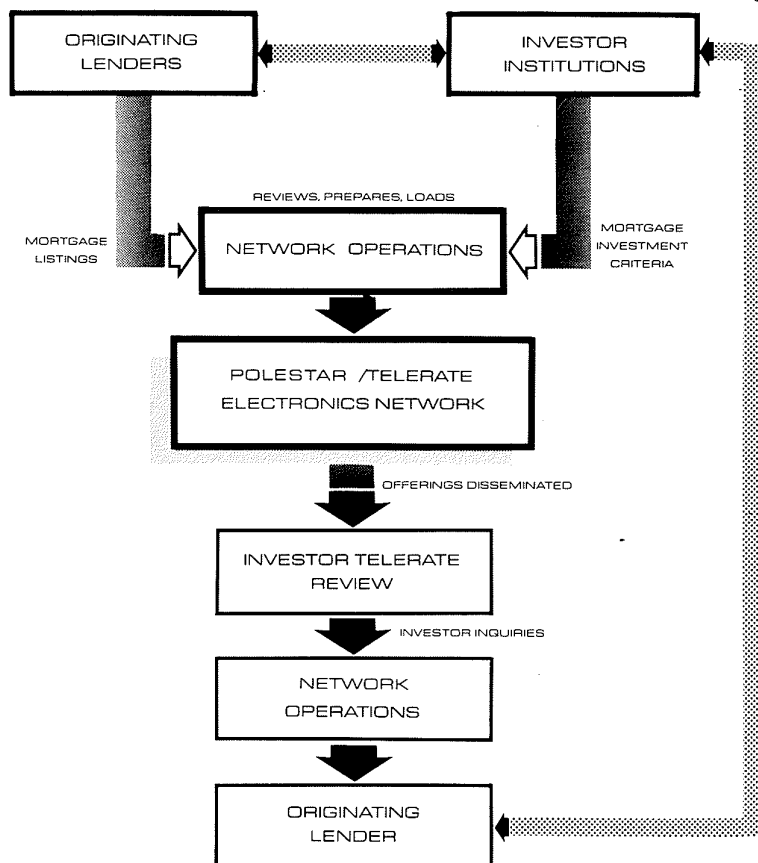
Nevertheless, the new system appeals to high-volume sellers and servicers as well, says Jenkins. With the personal computer system, they have more control over their data transmission and can easily make last-minute substitutions and changes.

The introduction of the new system has already increased the number of loans Freddie Mac receives electronically. Following the program's introduction in July, 30% of loan sales were delivered electronically, up from 25% in June. Reporting on loans, done through computer or direct computer linkage, jumped to 60% of total purchases by the agency, up from 50% in June.

In August, 30 institutions were using MIDANET for the personal computer. Users are being phased in gradually to make certain the software is working properly, says Jenkins. The systems have proved a great time-saver for institutions, he says. At one institution, MIDANET has reduced the time required to prepare the mortgage paperwork from 75 hours to one hour. In one recent loan purchase, 2,000 loans were delivered to Freddie Mac within seven minutes.

In another case last year, Freddie bought a \$1.6 billion package containing 35,000 loans. The seller estimated it would take six weeks to complete the forms manually. With the MIDANET software, the sale was completed in 10 business days, says Jenkins.

In June, Fannie Mae also introduced its own computerised accounting and purchase system based on



Flowchart for the Polestar system.

personal computers, known as MORNET. Currently, Freddie Mac's MIDANET system can be used with a wider variety of loan sales and transactions than MORNET, but Fannie Mae plans to expand its system. About 50 sellers are registered to use MORNET, according to Tom Harter, senior vice-president, customer and management information services, at Fannie Mae.

MORNET and MIDANET differ slightly. MORNET uses an electronic mail system supplied by the GTE Telenet System, while MIDANET has data transmitted directly to its computer over telephone lines.

The private companies

In addition to the computerised programs offered by the agencies,

private companies have sprung up offering to match buyers and sellers of packages of mortgages.

The Polestar System, introduced by the real estate firm of Blackman Garlock Flynn of San Francisco, matches buyers and sellers using computers, and then its personal staff steps in to arrange the transaction.

The Mortgage Monitor of American Mortgage Information Service in Santa Monica, California, acts as a classified ad service. For a subscription fee, the participants get access to its listings of offers to buy or sell loans.

Nationwide PRIME, a service of Nationwide Secondary Marketing of Fort Lauderdale, Florida, operates as private mortgage brokers. For a fee,

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participants list their deals with Nationwide exclusively and the company matches them up. Other systems, such as MORT of Scottsdale, Arizona, are very sophisticated computer systems connecting institutions to each other.

As volume continues to grow in the secondary mortgage market, the use of computers by the large agencies and by private companies should also grow.

Mortgage origination

The least computerised part of the mortgage business today in the US is mortgage origination. Savings institutions still wait for customers to walk through their doors, at which point the loan officers take applications by hand.

A number of computerised programs have been introduced over the past few years enabling real estate brokers and homebuyers to shop for a home mortgage in a broker's office. With a personal computer, or just a terminal, the broker can call up on the screen the mortgage quotes from a number of institutions.

Last year, the National Association of Realtors announced that its Rennie Mae mortgage information system could also be used to originate mortgages. Mortgage origination systems have also been launched by other

companies, but so far, the real estate brokerage community has not been enthusiastic about such systems.

However, new systems that connect the realtor's office directly with a mortgage institution itself are doing well, although they have only just been introduced. One is operated through the Realty World real estate brokerage franchise and MeraBank, a \$5.5 billion savings bank in Phoenix, Arizona. By becoming a franchisee of Realty World, a broker can use the ReaLoan mortgage origination program. A personal computer is installed in his office, directly connected to MeraBank's mortgage loan department.

With the ReaLoan program, the broker keys in the financial information about the mortgage applicant. The program will analyse the applicant's financial condition, tell him how expensive a house he can afford to buy, and then specify how the purchase would be affected by using any of the 40 different types of mortgages that MeraBank offers.

The broker and his customer can sit at the computer and play with different parameters, seeing how they change the mortgage or price of house the customer can buy. Once

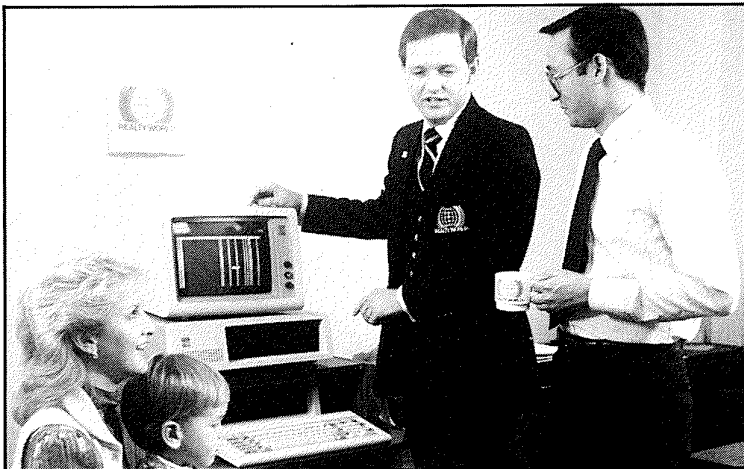
they select a loan, they can make the application on the computer. MeraBank will issue a commitment immediately, on condition that the data entered by the customer proves to be accurate and the appraisal proves to be satisfactory.

Currently, MeraBank has over 150 brokers attached to it through the ReaLoan system, and plans to have 800 in a few years. "We are a big institution and our mortgage rates are very competitive," says Dick Powell, head of the Realty World operation at MeraBank. "ReaLoan enables homebuyers in small- to medium-sized towns with small savings institutions to get the same competitive rates as people in big cities."

For example, ReaLoan enabled one broker in the small town of Sherman, Texas, to capture 8% of the town's residential mortgage business after just several months of being in business. Through ReaLoan, he could offer his customers better mortgage rates than they get from their local financial institutions.

Real estate brokers also like the program because they can tell immediately if the buyer is qualified for financing.

"ReaLoan will not replace human beings, but it makes processing and analysing a mortgage much easier," says Powell. "But to make this system work, you really have to invest a lot of time and money and be willing to work through the operational difficulties that arise. This is a brand new way of doing business for savings institutions. We really believe this type of computerised origination has great potential."



Prospective borrowers discuss their options helped by a computer linked to the ReaLoan system.

NATALIE McKELVY is a freelance financial writer based in Chicago. She is a former speechwriter for the US League of Savings Institutions. She is also the author of "Pension Fund Investments in Real Estate: A Guide for Plan Sponsors and Real Estate Professionals," published by Greenwood Press, Westport, CT in 1983. Ms McKelvy has worked as a journalist for "The Chicago Tribune" and "Pensions & Investment Age" magazine.