Govt Behind New Push For Banks to Make Home Loans to Those with Lower Credit Scores

April 3, 2013 - Edmund Burke said, "Those who don't know history are destined to repeat it." But Burke was talking about the events of prior generations. It probably never occurred to him that events only six years old would slip so easily from the minds of political decision makers. Unfortunately, that appears to be precisely what has happened as the Obama administration is now pushing banks to extend government guaranteed home loans to borrowers with lower credit scores. Could this be the beginning of the Great Recession - Part Deux?

Tweet

(function() {
var s = document.createElement('SCRIPT'), s1 = document.getElementsByTagName('SCRIPT')[0];
s.type = 'text/javascript';
s.src = 'http://widgets.digg.com/buttons.js';
s1.parentNode.insertBefore(s, s1);
})();

(function() {
var po = document.createElement('script'); po.type = 'text/javascript'; po.async = true;
po.src = 'https://apis.google.com/js/plusone.js';
var s = document.getElementsByTagName('script')[0]; s.parentNode.insertBefore(po, s);
})();

For anyone with short term memory issues who is in need of a quick refresher, the Great Recession began with a collapse in housing prices. That collapse was caused largely by the proliferation of home mortgages to people who had lower credit scores and little hope of ever being able to repay the amounts they had borrowed. And the vast majority of those loans were backed by Fannie Mae and Freddie Mac.

As a result of poor lending decisions at banks that offered Fannie and Freddie loans, both organizations became insolvent and wound up being taken over by the government. That left taxpayers on the hook. It also hurt every single homeowner who didn't default on their mortgage by reducing the price of their homes.

In the end, the federal government sued many lenders to recover some of the money that was lost as a result of their bad lending decisions. Now, jump six years.

Since Fannie and Freddie are now largely insolvent, the government has no plan to use them in this new lending push. Instead, it wants banks to start making loans to borrowers with mediocre credit through the FHA. Once again, these loans would be federally guaranteed. And once again, taxpayers would be on the hook.

So far, most banks have said "no" to this new scheme, largely because they are afraid of more lawsuits being filed against them by the government for making bad loans. But administration has not given up. In fact, it has doubled down by telling banks that as long as they adhere to FHA lending guidelines, they will not be sued.

Since the 2007 collapse in housing prices, getting a home mortgage has been much more difficult. Many banks won't lend to people with scores that are lower than 650. FHA guidelines allow for borrowing with credit scores as low as 500.

That's approaching the same type of loan underwriting standard as we had six years ago. And if this push gains traction, it is bound to lead to the very same results as those that we saw in 2007. That won't be good for anyone.

byJim Malmberg
Note: When posting a comment, please sign-in first if you want a response. If you are not registered, click here. Registration is easy and free.
Follow me on Twitter:

Follow ACCESS