

THE IMPORTANCE OF THE SECURITY PROPERTY IN RESIDENTIAL MORTGAGE LENDING

A crucial but often overlooked principle of primary market mortgage lending is the quality of the security property or “collateral.” After all, a long-term mortgage loan is a crucial element in delivering affordable housing to the masses – the great bulk of the households who cannot afford to pay out-of-pocket for the home of their dreams or even the home of their needs. Thus, a mortgage banker must know with some certainty that over the course of a twenty-year or even thirty-year period of time, the property which has been put at risk – the collateral property – will sustain its value in case the borrower defaults on the loan.

The drive to “affordability” has become fashionable in many circles. Too often this comes to imply that “cheaper” is preferred. Thus, the drive to reduce the cost of production to bare minimal levels has taken over the discourse. In our view, this is faulty and even dangerous.

In reality “housing affordability” in emerging markets is achieved through a combination of judicious project management and use of modern building technologies on the production side of housing, while addressing – and solving – the common dysfunctions in primary market mortgage lending on the financing side of housing, the “twin pillars.” We can achieve maximum affordability through: (i) improvement in the cost of production per square meter and employment of scale economics in production, while (ii) reducing interest rates through volume throughput and competitive forces and extending loan tenors through connection to local capital markets.

The illusion of achieving “affordability” becomes fashionable when emphasis is placed on reducing

production cost per square meter to unrealistically low levels such that the housing that is produced is not climate-resilient or wear-resilient nor is it “bankable.”

WHAT IS A RESILIENT AND BANKABLE PROPERTY?

The simple answer: a property on which a professional mortgage banker would be willing to make a long-term mortgage loan, using the property as collateral. Flimsy structures, poorly designed homes, structures that cannot withstand 30 years of normal wear-and-tear, or structures that cannot withstand the predictable ravages of storms, earthquakes and other natural disasters (climate resilient) cannot qualify as security properties. [Let’s put aside the ordinary hazard insurance policies that need to be obtained in the normal course of business as a risk management measure]. Location and physical environment are value-added attributes that must be considered in any valuation or underwriting of the property. An affordable home that is located within a nicely designed community with access to retail shopping, clinics, schools and community services, sustains its value more strongly over time and is much more valuable to the home owners from inception.

THE HOLISTIC SOLUTION ADDRESSES THIS PROBLEM

The holistic solution calls for an interaction and cooperation between the residential property developer and the focused, specialized and innovative mortgage lender. Volume throughput in both businesses is crucial for success of each. But quality is also a crucial success factor for both. The business relationship and mutual dependency ensures that bankable quality of homes will be produced.