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Can Unemployment Numbers Predict the Number of Mortgages That Will Go into Forbearance?

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Estimating how many mortgage holders will ask for forbearance in the coming months is critical. Regulators and Congress have, rightly, offered the 33.4 million mortgage holders with government-backed mortgages a six-month forbearance on their monthly payment if they need it, with the option to extend for an additional six months.[1]

But to avoid a widespread housing finance system failure that will make it hard for millions of families to buy homes once we recover (Kaul 2020), the government also needs to provide enough support to mortgage servicers, who must continue to pay investors even when mortgage holders do not make their payments.[2]

To determine how much support mortgage servicers need requires some estimate of the mortgage forbearance rate, which is not easy. Most mortgage market analysts have modeled homeowners' forbearance take-up on the unemployment rate. April's unemployment rate was 14.7 percent, and some economists predict it could exceed 20 percent in the coming months.[3] Meanwhile, the Mortgage Bankers Association's forbearance estimates were 7.91 percent as of May 3, but this is also likely to increase as May rolls on and June payments become due.[4]

But the relationship between forbearance and unemployment is complicated. It is important to get this right, but to do that, we need a robust discussion about the way we forecast forbearance. One place to start is to consider calculating the number of mortgages likely to take up the forbearance offer based on the homeowner unemployment rate, not the overall unemployment rate.

This is not a perfect solution. We offer three reasons the forbearance rate might be higher than the homeowner unemployment rate and three reasons it might be lower.

About the Mortgage Markets COVID-19 Collaborative

Initially convened in March 2020 by the Urban Institute, the Mortgage Markets COVID-19 Collaborative (MMCC) brings together a wide range of experts and stakeholders who share data and discuss how the mortgage market's response to the current pandemic can ensure equity, inclusion, and sustainability for homeowners

The COVID-19 public health crisis has created wide-ranging disruptions and a fast-moving economic downturn, with job losses and consumer hardships that are rippling through housing markets and crippling the housing finance system. Congress has quickly passed stimulus packages, and the major federal housing agencies have enacted federal and state forbearance and foreclosure and eviction moratoriums to help homeowners struggling to make their mortgage payments during this pandemic. In addition, the Federal Reserve and the US Department of the Treasury are taking actions to bolster the housing market by buying mortgage-backed securities at unprecedented levels and creating vehicles to bring liquidity to the mortgage servicing system that supports more than 48 million homeowners with mortgages.

This crisis has the potential to be more disruptive and far reaching than the 2008 crisis, with different implications and ramifications, given its potential length, national scale, unemployment projections, and loss and default projections.

The housing crisis in 2008, natural disasters, and similar incidents have taught us that aligned, coordinated, and intentional engagement by mortgage industry, nonprofit, and consumer groups is critical to developing and implementing thoughtful, evidence-based, and effective policies and practices that will mutually benefit consumers and the mortgage industry.

The MMCC seeks to

- produce a shared repository of data, research, and policy proposals; and
- increase understanding among all participants of the existing data and research and of the concerns and perspectives of other industry and community stakeholders.

For more information about the MMCC or to see the list of collaborators and research assembled, visit the program page at http://www.urban.org/policy-centers/housing-finance-policy-center/projects/mortgage-markets-covid-19-collaborative.

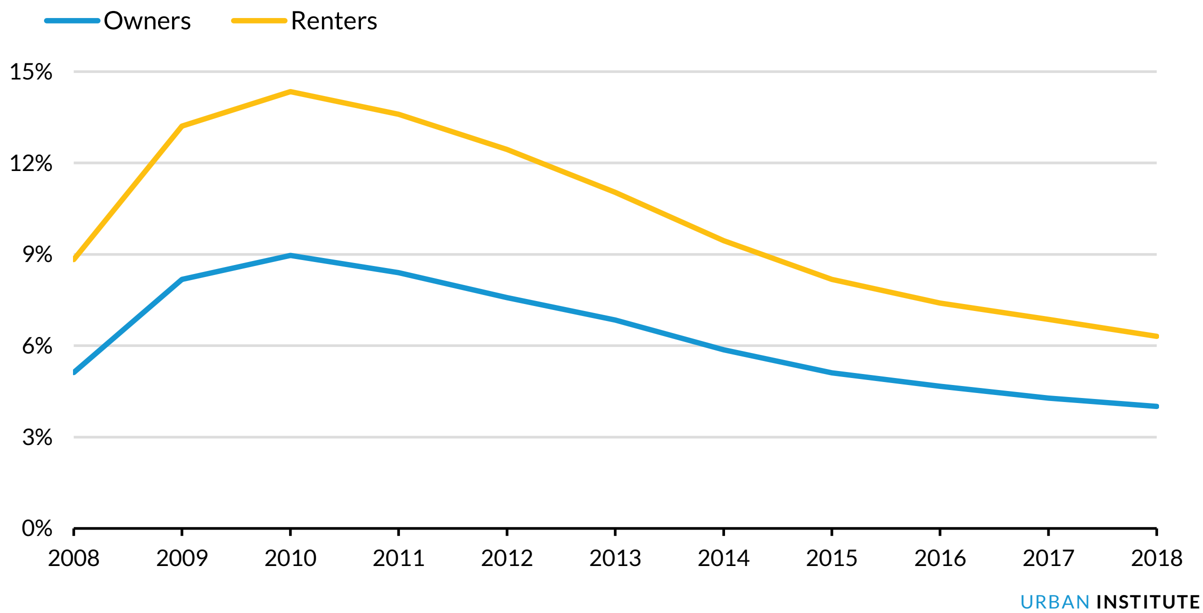
We Should Base Mortgage Forbearance Estimates on the Consistently Lower Homeowner Unemployment Rate

The homeowner unemployment rate is consistently lower than the renter rate—generally about 62 percent of the renters' rate and about 80 percent of the total unemployment rate.

The just-released April unemployment rate is 14.7 percent, and assuming this will be the unemployment rate for the second quarter of 2020 (higher in May, lower in June) and that the historical relationship holds, the homeowner unemployment rate for the second quarter was likely 11.8 percent. And the unemployment gap between homeowners and renters will likely be higher during the pandemic because renters are more concentrated in industries more vulnerable to the COVID-19 shock (HFPC 2020).

FIGURE 1

Unemployment Rate by Housing Tenure



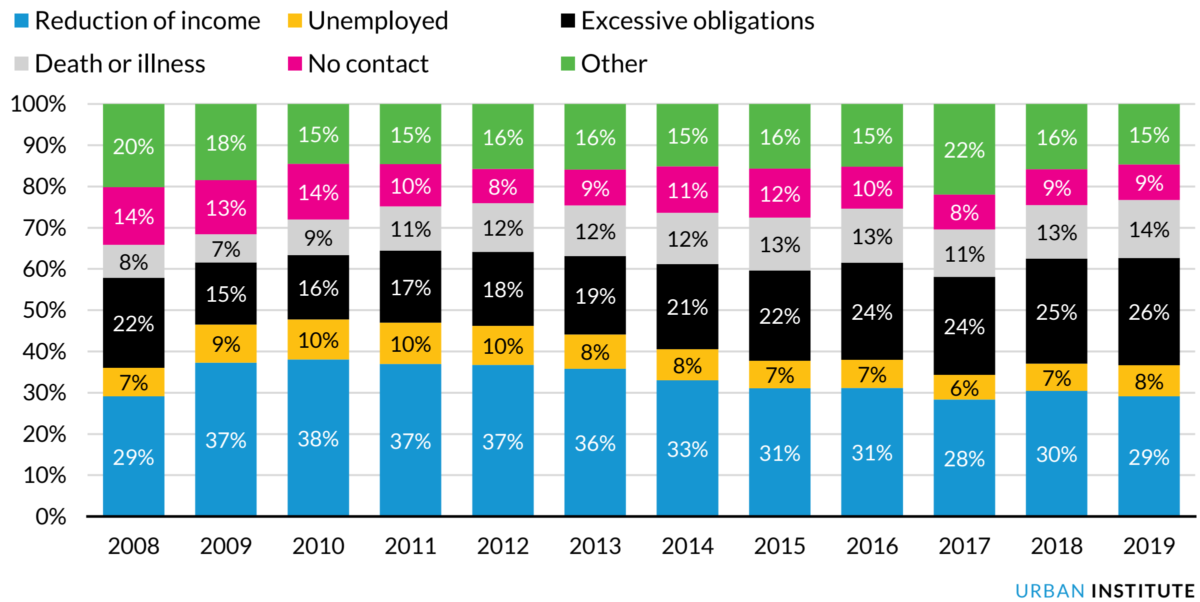
Source: American Community Survey.

Three Reasons the Forbearance Rate Could Be Higher Than the Homeowner Unemployment Rate

1. **Borrowers who were experiencing financial hardships before COVID-19 will likely seek forbearance under the Coronavirus Aid, Relief, and Economic Security (CARES) Act.** Even during good times, some borrowers cannot make their mortgage payments. In 2019, only 37 percent of Federal Housing Administration 90-day delinquencies were based on employment loss or other income reduction. The rest were based on excessive obligations, death or illness, marital difficulties, or other reasons. Some of these borrowers may opt to take advantage of the forbearance option, which does not require proof of unemployment or income reduction.

FIGURE 2

Reasons for Federal Housing Administration Loans Being 90 or More Days Delinquent



Source: Authors' calculations of US Department of Housing and Urban Development data.

2. **Many people who have lost some income do not qualify for unemployment.** Although some states have a concept of partial unemployment, the rules generally require workers to earn less than they would in unemployment benefits if they were fully unemployed. This is a fairly low number, as unemployment benefits on average replace about 50 percent of a worker's income, up to a cap.[5] And the additional $600 weekly benefit does not count toward this threshold.[6] Historically, loss of income has been a more important contributor to default than unemployment. In 2019, of the 37 percent of mortgage holders that went delinquent because of employment or income loss, 29 percent were caused by an income reduction and only 8 percent were caused by unemployment. Over time, 80 percent of total delinquencies caused by reduction of income or unemployment are caused by loss of income.

3. **Moral hazard**. The CARES Act does not require borrowers to submit documentation to verify a hardship, though borrowers must attest that they are having financial difficulties. This might persuade some who think they might be unemployed in the future to seek forbearance, as there is no penalty for doing so. Borrowers do need to pay back the forborne amount, but if it can be deferred to the end of the life of the loan, the present value is about 35 cents on the dollar.

Three Reasons the Forbearance Rate Could Be Lower Than the Homeowner Unemployment Rate

1. **Even unemployed homeowners may be in a good position to pay their mortgage**. The American Community Survey shows that at $93,000, the median family income of homeowners with a mortgage is much higher than the median family income of homeowners without a

mortgage ($55,000) or of renters ($41,000). Many homeowners have savings or can tap into their home equity to make their payments. Unlike during the Great Recession, households today have a lot of equity in their homes, which provides a greater buffer to weather financial difficulties, though tapping into home equity may be challenging as credit tightens during the COVID-19 crisis.[7]

2. **CARES Act payments plus boosted and base unemployment benefits may replace lost wages entirely, allowing many unemployed homeowners to make their mortgage payments.** Although this is not true for the median homeowner, it is true for those at the 25th percentile. Texas homeowners at the 25th percentile of homeowners with a mortgage earned $56,000 year, or $4,667 a month. Unemployment benefits (half of the gross income, subject to a cap) plus $600 a week total $4,854 a month, leaving the 25th-percentile borrower better off by $187. Although the results vary by state, the differences are reasonably small in most. But not all who qualify actually receive unemployment benefits. A recent survey found that for every 10 successful applicants, 3 or 4 more tried but could not get through the system, and 2 gave up applying because it was too difficult.[8] In addition, some states have not yet expanded their programs to include self-employed workers or those in the gig economy, both newly covered by the CARES Act.[9]

TABLE 1

How Important Is Unemployment Insurance in Filling the Income Gap for Homeowners with a Mortgage?

10 most-populous states

	Homeowners with Median Household Income				Homeowners at the 25th Household Income Percentile			
State	Annual HH income ($)	Monthly HH income ($)	Estimated UI benefit + CARES $600/week ($)	HH income minus total benefit ($)	Annual HH income ($)	Monthly HH income ($)	Estimated UI benefit + CARES $600/week ($)	HH income minus total benefit ($)
CA	111,300	9,275	4,547	4,729	65,000	5,417	4,547	870
TX	95,000	7,917	4,854	3,063	56,000	4,667	4,854	-187
FL	79,900	6,658	3,789	2,870	45,700	3,808	3,789	20
NY	107,600	8,967	4,811	4,156	63,400	5,283	4,811	473
PA	89,730	7,478	5,109	2,368	54,000	4,500	4,848	-348
IL	95,500	7,958	4,764	3,194	57,300	4,775	4,764	11
OH	83,000	6,917	5,400	1,517	50,000	4,167	4,681	-515
GA	88,000	7,333	4,178	3,155	50,500	4,208	4,178	30
NC	80,800	6,733	4,114	2,620	48,000	4,000	4,114	-114
MI	82,100	6,842	4,165	2,676	49,600	4,133	4,165	-32

Sources: American Community Survey and Bureau of Labor Statistics.

Note: CARES = Coronavirus Aid, Relief, and Economic Security; HH = household; UI = unemployment insurance.

3. **The unemployment rate does not take dual incomes into account.** The unemployment rate is calculated for individual workers, but the mortgage is paid by a household. If one borrower has lost his or her job, but the coborrower has not, the family may still be able to pay the mortgage. Homeowners are more likely to be married and have dual incomes than renters, so some households may be able to continue paying their mortgages, with an assist from unemployment benefits, even when a member of the household loses a job (Choi et al. 2018).

There is a clear relationship between forbearance and the homeowner unemployment rate, but many other factors will determine the amount of forbearance. Some factors could push forbearance take-up above the unemployment rate, while others could reduce it. Their net impact is not immediately clear. Current evidence from the Mortgage Bankers Association showing the slowing growth of forbearance in the last few weeks suggest forbearance may be lower than the homeowner unemployment rate.[10]

Why This Matters

Servicers are responsible for advancing principal and interest payments on government-sponsored enterprise loans for the first four months of the forbearance and are responsible for real estate taxes, insurance, the private mortgage insurance premium, and guarantee fees during the entire forbearance period, even if they do not receive it from the borrower. Servicers on Ginnie Mae loans must advance principal and interest, taxes, insurance, and the mortgage insurance premium. They may opt to tap Ginnie Mae's Pass-Through Assistance Program for principal and interest advances, but the borrowing rate is higher than for most alternatives.[11]

The prospect of forbearance and its implications for servicers' liquidity, particularly that of nonbank servicers, has likely already contributed to tightening credit availability and could affect the recovery, particularly if credit standards are further tightened because many originators or servicers exit the market.[12]

Notes

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