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COVID-19 and the US Mortgage Industry: Social Distancing Paves the Way for Digital Proximity

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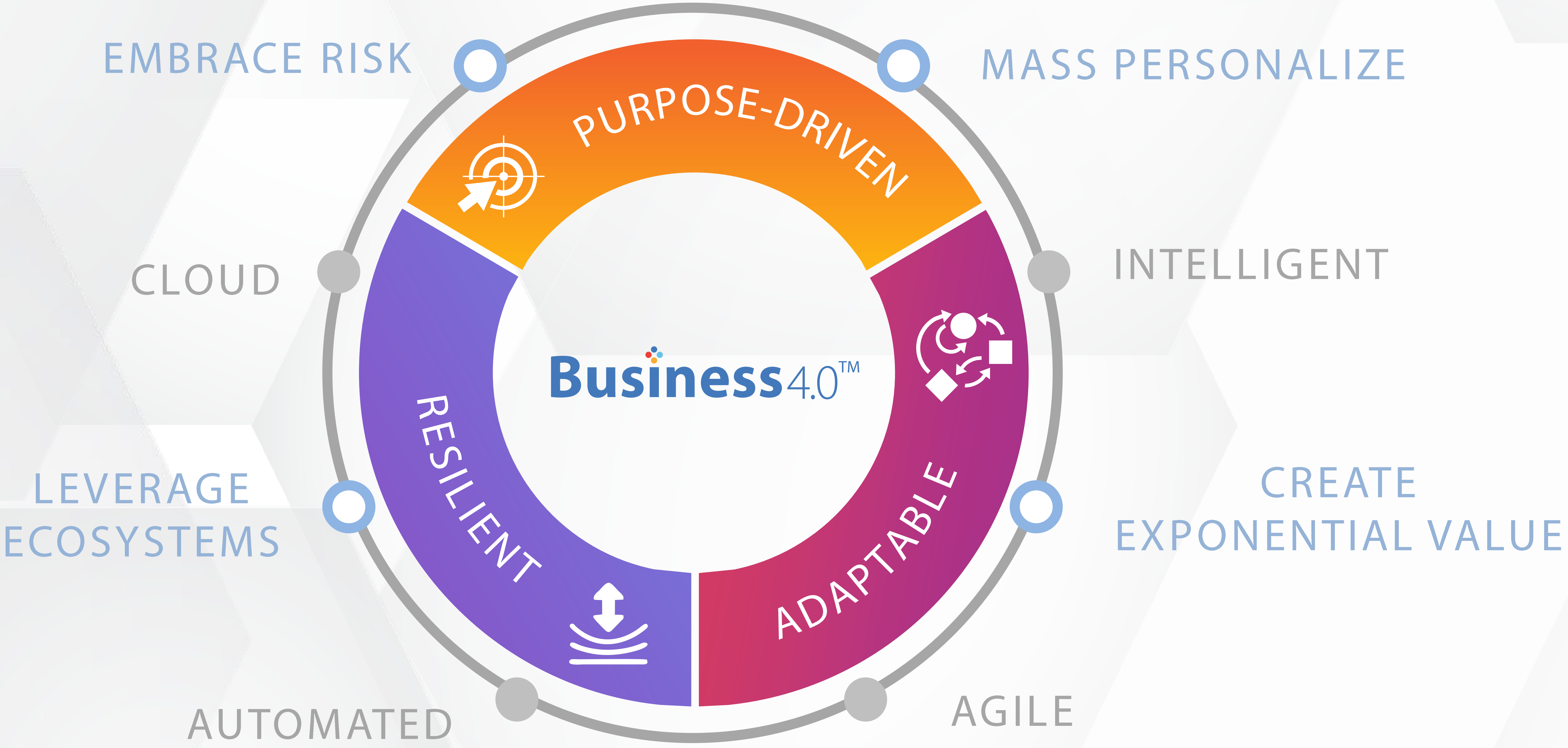

About the Authors

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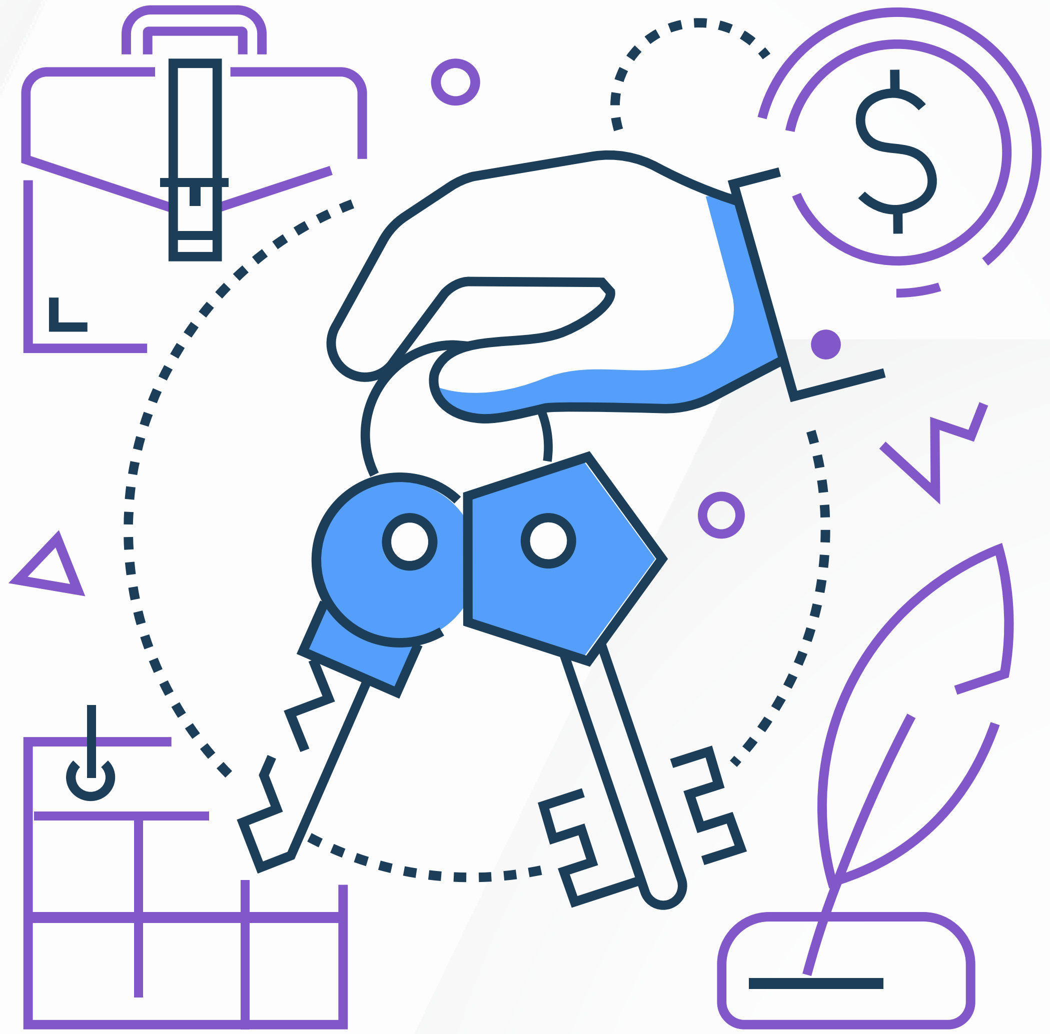
Abstract

The COVID-19 pandemic has brought about widespread uncertainties and unknowns for the mortgage market. The pandemic has created both macroscopic and microscopic issues for every industry including the human-sensitive and people-centric mortgage industry.

This white paper highlights the COVID-19 impact on the US mortgage industry and its operating models as well as how the impact on people, process, and technology can be addressed. We also discuss how the traditional mortgage industry is ripe for disruptive innovation leveraging agile methodologies and digital technologies.

Mortgage Industry: Current State of Affairs

Mortgage is the most complex banking product offered in innumerable flavors. The business models of institutions offering mortgages, ways of funding, types of structuring, and kinds of stakeholders are all completely different across geographies. Of these, the US mortgage market is one of the most complex and the largest with outstanding debt standing at USD 15.8 trillion.[1] The fourth quarter of 2019 was the most profitable last quarter of the year since 2012 for independent mortgage banks according to a quarterly survey.[2] Most production and servicing respondents reported profits – in short, the industry was at a peak with low delinquency rates, higher origination, and increased profitability.

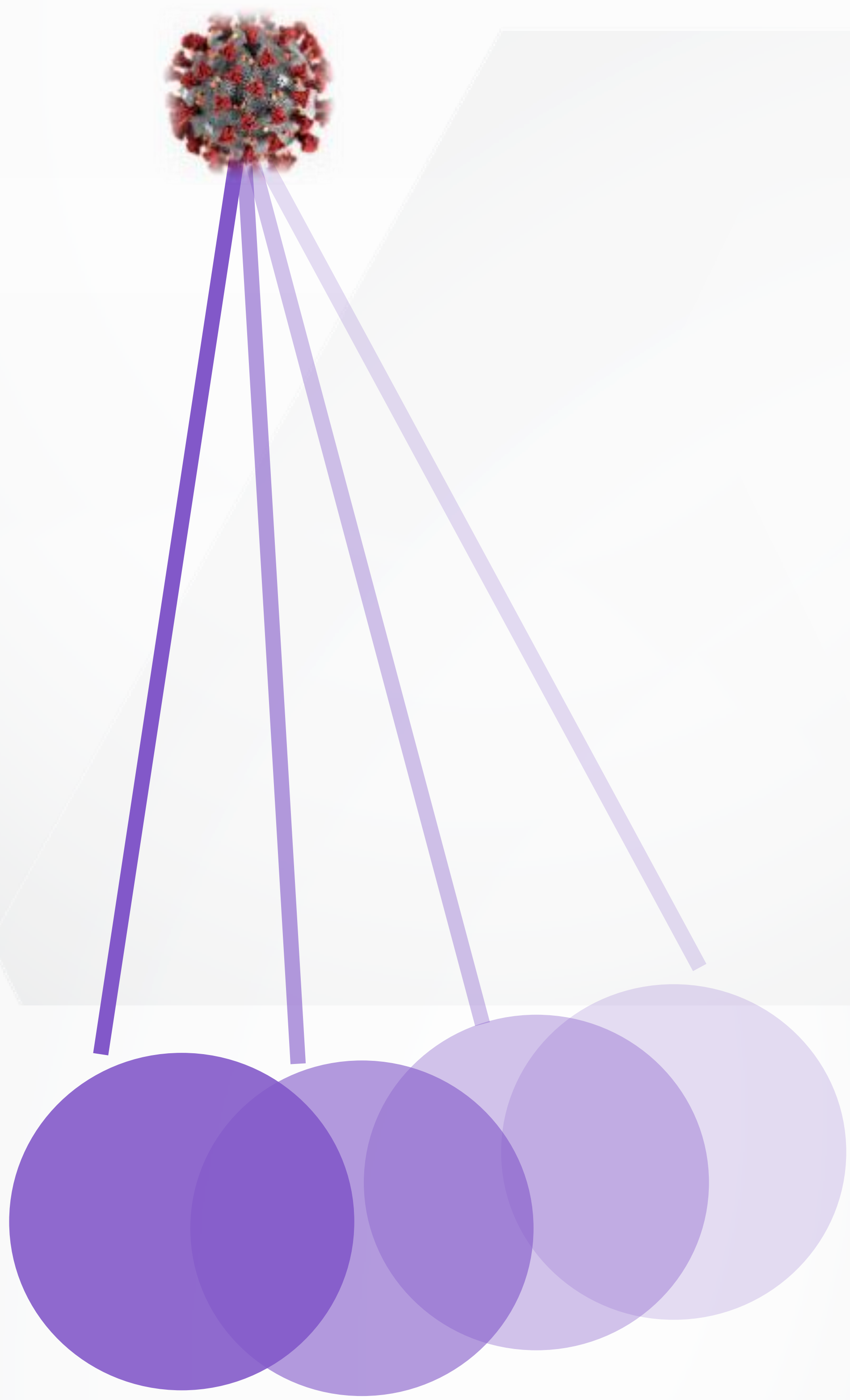


By March 2020, the COVID-19 outbreak had spread to all 50 states in the US and started significantly impacting the housing industry, as unemployment constrained new home purchases and repayment of existing loans. The US mortgage industry has embraced innovation in the wake of the crisis by incrementally exploring the possibilities of introducing video-based closings, drones, robot and 3D imaging-based appraisals, remote online notarizations (RONs), remote ink-signed notarizations (RIN), and so on. In addition, regulators as well as investors like government-sponsored enterprises (GSEs) are easing restrictions to reduce business interruptions.

[1] HW, U.S. mortgage debt hits a record $15.8 trillion, Jan 2020, Accessed June 2020, https://www.housingwire.com/articles/u-s-mortgage-debt-hits-a-record-15-8-trillion/

[2] Mortgage Bankers Association, IMBs Post Strongest Fourth Quarter Profits Since 2012, Mar 2020, Accessed June, https://www.mba.org/2020-press-releases/march/imbs-post-strongest-fourth-quarter-profits-since-2012

Pre and Post COVID Shift



New 'eligible' borrower

Average credit score **580+***

Employment verification **120 days***

Jumbo loans and non-qualified mortgage

Average credit score **660+***

Employment verification in **10 days***

Jumbo loans suspended

Slowdown of non-qualified mortgage

Digitization of ecosystem

Full appraisal

Manual upload of property photos

Low adoption of e-notaries

Physical document recording

Outside-the-box appraisals - exterior only

Augmented by satellite imagery and street views

Video, Facetime, Skype, RIN, RON notarizations

Over 100 million documents e-recorded (Simplifile)

Remote, yet proximate employees

%-10% Workforce working from home

Remote working on the rise in mortgage firms (Quicken Loans, Wells Fargo, JPMorgan Chase)**

Employees working on mission critical processes only to enter worksites (Fannie Mae)**

Macro Economics

50-60,000 jobless claims a week ***

3-4% unemployment rate ***

350-400,000 jobless claims a week***

13-14% unemployment rate***

8.55% loans in forbearance****

Figure 1: Quick Snapshot of Pre and Post Covid-19 Scenarios in US Mortgage Industry

* Housing Wire, Mortgage lenders tightening standards as coronavirus crisis worsens, Apr 2020, Jun 2020 https://www.housingwire.com/articles/mortgage-lenders-are-tightening-standards-as-coronavirus-crisis-worsens/

** Housing Wire, Here's how the mortgage industry is reacting to the corona virus, Mar 2020, Jun 2020 https://www.housingwire.com/articles/heres-how-the-mortgage-industry-is-reacting-to-the-coronavirus/

*** Department of Labour, Unemployment Insurance Weekly Claims, Jun 2020, Accessed Jun 2020, https://www.dol.gov/ui/data.pdf

**** MBA, Share of mortgage loans in Forbearance Increases to 8.55%, Jun 2020, Accessed Jun 2020 https://www.mba.org/2020-press-releases/june/share-of-mortgage-loans-in-forbearance-increases-to-855#:~:text=WASHINGTON%2C%20D.C.%20(June%2016%2C,as%20of%20June%207%2C%202020.

New ‘Eligible’ Borrower

As risk appetite takes a temporary beating, lenders are tightening mortgage rules and standards. Non-qualified mortgage (NQM) loans, a hot product in 2019, is witnessing a downtick. Home equity lines of credit (HELOCs) are on hold and jumbo loans are suspended. Lenders are adopting stricter norms to identify ‘eligible’ borrowers – they are playing safe by preferring customers with high credit scores and insisting on higher down payments to avoid defaults later. GSEs continue to monitor and adopt policies based on the risk tolerance of borrowers.

Industry influencers believe that most of the post COVID-19 crisis disruptions will be in the income and employment aspects of the credit engine. Economic disruptions will be more regional. On a positive note, markets are still holding strong, which can be attributed to the right fundamentals being in place, a strong supportive interest rate environment, and stable home prices. That said, borrowers need help, and lenders’ product policy decisions will be key determining factors in supporting borrowers through the crisis.

Digitalization' of Ecosystem Providers

The US mortgage industry spans a huge ecosystem of vendors across all areas including appraisal, title, insurance, brokers, escrow, taxes, flood, credit, and so on. Since entering the sector in 2012, fintechs have been playing a major role in the digitalization of the mortgage process. Technology investments have been going up over the last few years with 2020 being touted as the year of the mortgage application programming interface (API). However, COVID-19 has altered the situation -- appraisal requirements are now relaxed and remote notarization through digital modes is accepted, as evidenced by Simplifile LC processing its hundred millionth document for e-recording in April 2020.[3]

While digitalization and customer communication will play a big role in the prevailing 'low-touch' or rather 'no-touch' environment, we believe that borrowers will always need a trusted advisor. This can be attributed to the fact that currently, digitalization is advanced in the initial customer facing areas but not so much in the closing stages. The solution lies in providers adopting technologies like APIs, augmented reality (AR) and/or virtual reality (VR), drones, robotic process automation (RPA), artificial intelligence (AI) and machine learning (ML) in key mortgage areas such as property valuations, mortgage document data extraction, customer communications, and so on. In addition, establishing a central repository for property data will help avoid duplication of data and ensure data integrity and real-time availability to all stakeholders in the ecosystem.

[3] Simplifile, Simplifile Processes Its 100 Millionth Document for E-recording, April 2020, Accessed June 2020, https://simplifile.com/about-simplifile/simplifile-news-and-press/press-releases/simplifile-processes-its-100-millionth-document-for-e-recording/

Evolution of ‘Fully Digitalized’ Mortgages

The digital lending platform market in North America is expected to register a compounded annual growth rate (CAGR) of 19% in 2019-25.[4] Our experience reveals that lenders have predominantly implemented digital solutions at the application stage but digital adoption is limited in the closing stages of the mortgage value chain. Many lenders are struggling as their existing monolithic core loan origination solutions (LOS) are a major barrier to integration through open APIs and digitalization.

In our view, there exists a lack of clarity in understanding the concept of ‘fully digitalized mortgage’ as the definition varies across stakeholders. Despite every stage of the mortgage lifecycle having digitalization potential, many processes such as hazard, flood, and title are yet to join the digital club. End-to-end digitalization of the mortgage value chain will help lenders collect all kinds of data apart from the traditional, transactional or performance parameters. Appropriate utilization of data insights can greatly enhance customer experience.

[4] Businesswire, Report on the North America Digital Lending Platform Market (2019-2025) - CAGR of 19% Expected During the Forecast Period - ResearchAndMarkets.com, Feb 2020, Accessed June 2020, https://www.businesswire.com/news/home/20200213005365/en

Remote yet 'Proximate' Employees

Our interactions with clients reveal that a majority of financial services professionals are of the view that remote working is proving to be effective. The US mortgage industry is not new to remote working and training; however, the scale of remote working necessitated by the pandemic is unprecedented and is fast becoming an accepted reality. Remote hiring is also working successfully. Digital tools are enabling employees to collaborate better and ensure uninterrupted service to mortgage customers – these tools are successfully overcoming the challenges imposed by social distancing norms. However, remote working also comes with certain challenges – for instance, fixing accountability, performance management, personal insecurities around not being connected to the team, and employees being head-hunted by the competition. Despite these problems, the trend is catching on; several mortgage lenders such as Quicken Loans and GSEs such as Fannie Mae and Freddie Mac are allowing employees to work remotely to ensure they stay safe.[5] While the crisis has created several new ways of operating, only time will tell which will stay viable and permanent.

[5] HW, Here's how the mortgage industry is reacting to the coronavirus, Mar 2020, Accessed June 2020, https://www.housingwire.com/articles/heres-how-the-mortgage-industry-is-reacting-to-the-coronavirus/

The Way Forward

The COVID-19 crisis is a warning bell for the mortgage industry urging firms to keep policies and procedures flexible and minimize the dependence on manual effort to ensure business certainty. This underscores the need for mortgage lenders to digitalize the end-to-end mortgage value chain.

Given increasing consumer adoption of digital modes of interaction, digital mortgage is no longer a nice-to-have. By leveraging the latest state-of-the-art technologies, mortgage lenders can do away with cumbersome, manual, error-prone, and paper-intensive processes, which in turn will drastically raise the customer experience quotient. Some areas where technology can significantly enhance the mortgage function include document management, data management, and customer service. Artificial intelligence (AI) and machine learning (ML) backed solutions can make document management more efficient while blockchain solutions can be used to ensure the security and integrity of distributed data in real time without the need for intermediation.

Similarly, adopting analytics frameworks can help improve customer service by predicting evolving customer needs. Enhancing customer experience to strengthen brand stickiness will hinge on banks' ability to anticipate the needs of individual customers and proactively create offerings personalized to meet them. Building ecosystems that satisfy the purpose or the need that drives customers – buying a home rather than a mortgage – and bringing together all the stakeholders required to meet varied needs on a single platform can go a long way to create customer delight. For instance, mortgage firms can look at creating a platform that includes property insurers, retailers offering home décor products, landscape architects, and so on. Such purpose-driven ecosystems will serve as a one-stop-shop for all customer needs – home buying, in this example – in turn exponentially raising the customer experience quotient and building a loyal customer base. Enabling variations in the product as well as pricing to support the unique needs of individual borrowers and differentiated customer journeys will demand flexible and agile digital processes with automated workflows and exception handling. Flexible product pricing policies and the ability to quickly introduce products in the market will become crucial to retaining an edge, which will necessitate the adoption of agile digital operating models.

The COVID-19 crisis has created several possibilities and accelerated digitalization efforts in the US mortgage industry. The government and regulators are being supportive through an easier interest rate environment and flexible policies; lenders should leverage this momentum to accelerate their digitalization roadmap, simplify processes, and streamline offerings and pricing. In addition, lenders should prepare to handle new scenarios, new types of borrowers, and changing expectations by moving away from product-centric business models to customer-centric, purpose-driven, and ecosystem based models.

Contact

For more information on TCS' Banking & Financial Services,
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About Tata Consultancy Services Ltd (TCS)

Tata Consultancy Services is an IT services, consulting and business solutions organization that delivers real results to global business, ensuring a level of certainty no other firm can match.

TCS offers a consulting-led, integrated portfolio of IT and IT-enabled infrastructure, engineering and assurance services. This is delivered through its unique Global Network Delivery Model™, recognized as the benchmark of excellence in software development. A part of the Tata Group, India's largest industrial conglomerate, TCS has a global footprint and is listed on the National Stock Exchange and Bombay Stock Exchange in India.

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