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Growing Mortgage Sales in a Diminished Purchase Market

The market for residential real estate in the U.S. endured a major contraction in 2013 when the largest mortgage refinancing boom in history came to an end. Mortgage lenders, accustomed to the comparatively easy revenues generated through loan refinancing, suddenly found themselves forced to compete aggressively for homebuyers seeking purchase loans. For most retail banks, the change presented major challenges. Sales skills had in many cases grown rusty, and hard-won real estate industry contacts had been lost through attrition.

For mortgage lenders in any market, the first key to success is strong relationships with local real estate agents, but this is particularly important during market contractions when competition is more intense. Given the vital importance of the lender-agent bond, lenders need to focus on establishing and maintaining these strong ties over the long term.

Major shifts in homebuyer markets

The third quarter of 2013 saw 30-year fixed-interest rates for mortgages climb from 3.54 to 4.49 percent.[1] This increase of 95 basis points marked the end of the largest refinance boom in U.S. history (Exhibit 1, page 2).

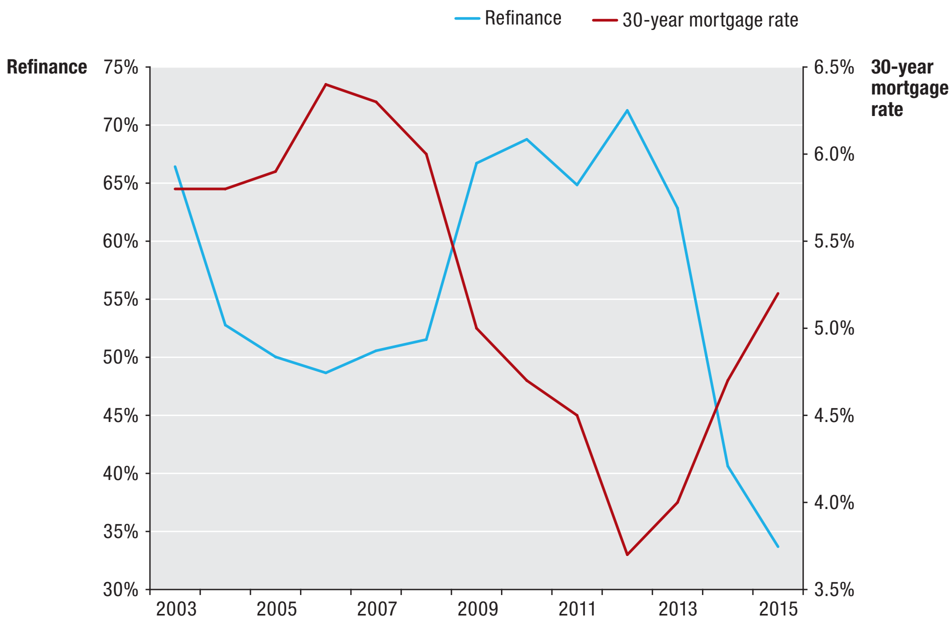
The uptick's impact was immediate. The U.S. real estate market rapidly began to contract. While originations in 2012 peaked at $2.1 trillion, the Mortgage Bankers Association (MBA) expects lenders will struggle to generate even $1 trillion of originations in 2014. By year's end, half of the originations market will have evaporated (Exhibit 2, page 2).

A 50 percent market contraction hits any industry hard; however, the mortgage market not only contracted, but was also reshaped in other ways. Fully 70 percent of

[1] Freddie Mac Primary Mortgage Market Survey.

Exhibit 1

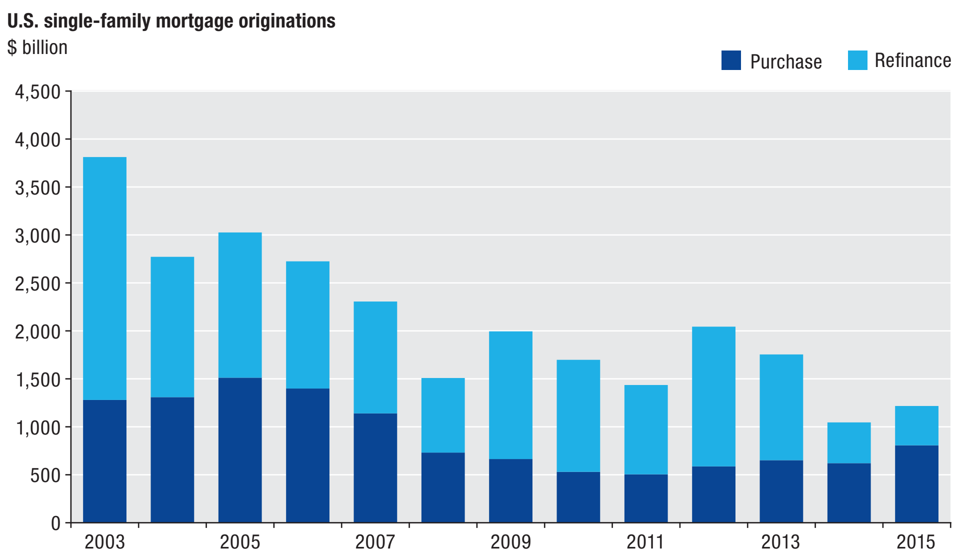
30-year fixed-interest rates for mortgages climbed 95 basis points in the third quarter of 2013



Source: Freddie Mac Primary Mortgage Market Survey

Exhibit 2

In 2014, the decline in mortgage originations is expected to be severe



Source: Mortgage Bankers Association

2012's bumper originations crop actually represented *refinanced* mortgages. By contrast, 80 percent of originations in 2015 are expected to be *purchases,*[2] and originations are expected to remain purchase-heavy for some time thereafter. This is significant because purchase loans are harder to originate because they require finding and coaching homebuyers, which is considerably more challenging than mining loan-servicing portfolios for streamlined Home Affordable Refinance Program (HARP) refinances. Additionally, as lenders struggle with fulfillment overcapacity during volume downturns, profit margins collapse.

[2] Purchase share projections vary: 65%, 75%, and 80% based on current forecasts by the Mortgage Bankers Association, Fannie Mae, and Freddie Mac, respectively.

During the financial crisis and the refinancing boom that followed, the industry lost a generation of seasoned mortgage loan officers (MLOs), largely through attrition. These MLOs and mortgage brokers, who were adept at self-sourcing leads and shepherding transactions through to closing, left the business in large numbers. Many of those who remain are out of practice at sourcing and closing purchase transactions. Consequently, distributed sales organizations have been struggling to keep MLO productivity high and origination pipelines flowing.

One essential group of actors has not left the stage, however. Real estate agents remain as influential as ever and still refer more purchase transactions to lenders than any other source. Second only to borrowers, agents effectively are the most critical bank customers.

Understanding the small, purchase-dominated market

Finding and capturing unmet demand in a diminished market is more crucial than in larger, refinance-dominated markets. A 50 percent market contraction within two years is extraordinarily disruptive. Mortgage employment has already declined by tens of thousands, M&A activity has grown, and weaker players have left the market. With an 80 percent purchase market, this effectively means that every channel must now be a purchase channel.

Being MLOs' primary source of borrower referrals, real estate agents are one of the three most important stakeholders in the purchase transaction. Homebuyers, real estate agents, and MLOs therefore need to work in close harmony. While each has different needs, those needs are tightly intertwined.

> Because they educate and guide customers through much of the home-buying process, real estate agents typically hold the lead position in the customer relationship.

Given the high stakes involved in real estate transactions, addressing the needs of all three groups can be challenging. Because they educate and guide customers through much of the home-buying process, real estate agents typically hold the lead position in the customer relationship. This means they are also one of the first people to whom homebuyers turn for recommendations—especially when the buyers are new to the area. Along with customers and MLOs, real estate agents should therefore be a prime focus of lenders' stakeholder-satisfaction programs.

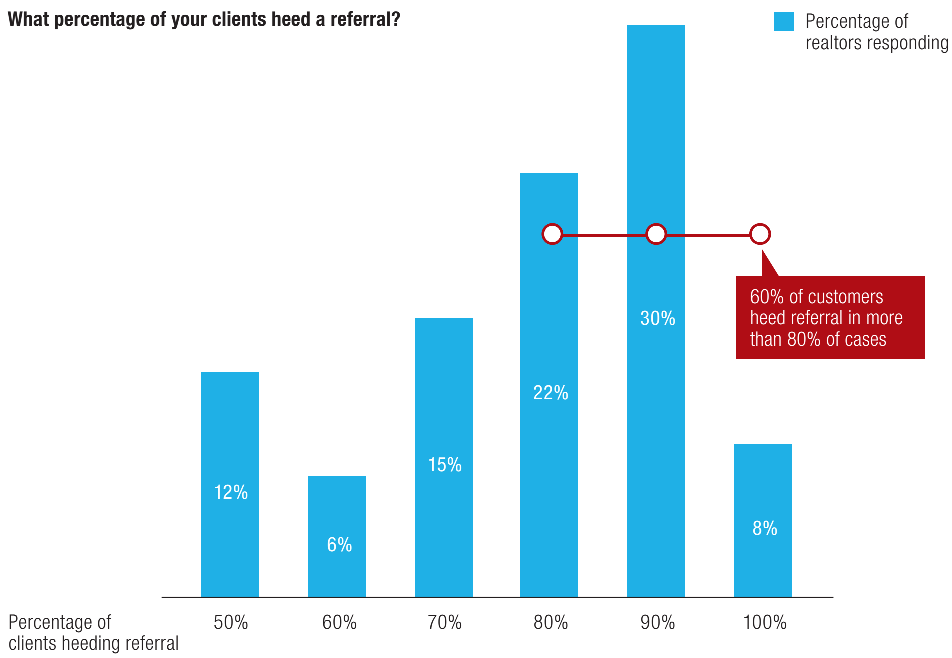
Maintaining strong working relationships with real estate agents accomplishes two lender objectives simultaneously. First, referrals from agents can supply a critical mass of prospective purchase borrowers, thus keeping fulfillment pipelines flowing during down markets. Secondly, delivering on the needs of agents also indirectly satisfies borrowers' needs, which dramatically improves customer satisfaction.

By the numbers

Despite fundamental economic, regulatory and demographic shifts, the influence that real estate agents exert in the mortgage selection process remains undiminished. In a McKinsey survey of more than 900 members of Trulia's online Active Rain community

Exhibit 3

When realtors refer a mortgage loan officer to their clients, the clients usually listen



Source: McKinsey/Active Rain Realtor survey

(real estate's largest professional social network), 95 percent of respondents said they recommend specific loan officers to their clients. These are not casual referrals. Most agents refer buyers to only a handful of MLOs. More than half refer to only two loan officers—and agents' opinions really matter. More than 90 percent of agents say their clients follow through on their referrals at least half the time, and 60 percent say borrowers choose the recommended MLO four out of five times (Exhibit 3).

Getting on the preferred lists of real estate agents is vital for MLO success, but for newcomers, doing so can be a major challenge: over 60 percent of agents in McKinsey's survey say they rarely, if ever, add new MLOs to their rotation lists.

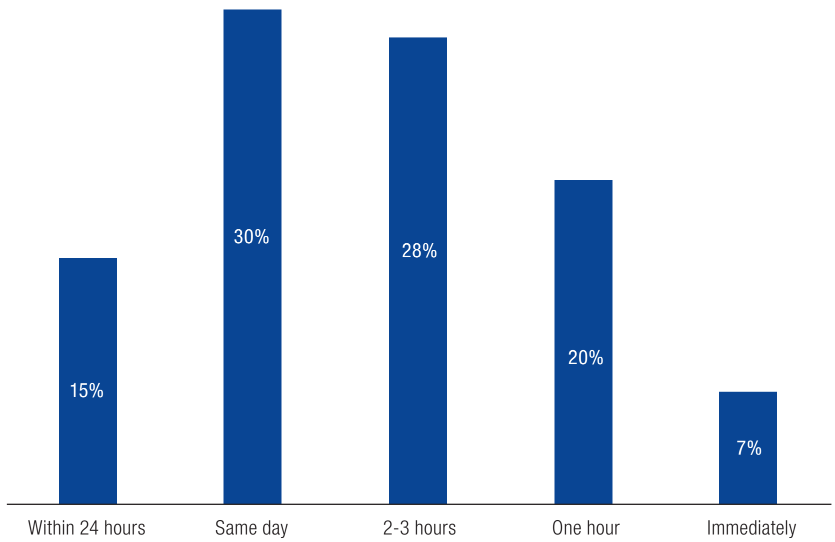
Earning a coveted spot

If real estate agents are key stakeholders in the deal, what does this mean for lenders? Simply stated, it means that the successful lenders will be those who closely align their value propositions with agents' needs and expectations. And what agents seek from MLOs differs somewhat from what homebuyers seek. Agents look for value, performance and superb communications above all else. McKinsey research found 55 percent of agents expect lenders to return their calls or emails within a few hours, at most. Agents get paid only if the loan closes, and in competitive markets where multiple offers are made on desirable properties, minutes matter. Prompt replies to questions about loan status and documentation can therefore be critical. It is little wonder then that survey results show 78 percent of agents expect same-day responses, and 20 percent expect callbacks within an hour. Notably, agents expect similarly prompt responses from MLOs to their borrowers' questions (Exhibit 4, page 5). More than half of agents surveyed said they only work with MLOs who are highly responsive on a consistent basis.

Exhibit 4

Real estate agents value quick response from mortgage loan officers

How quickly should MLOs respond to realtor calls/emails, or calls from a referred client?



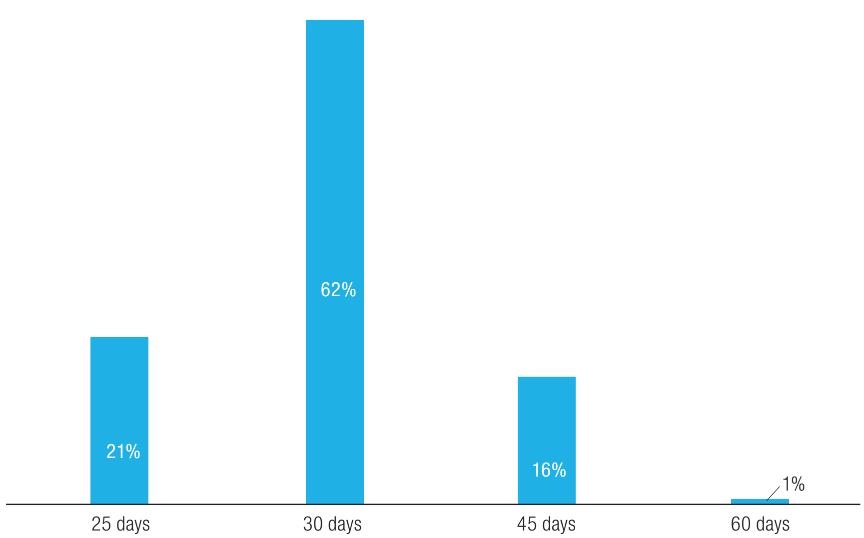
Source: McKinsey/Active Rain Realtor survey

Cycle times and closing dates are also important agent considerations. Most agents surveyed said that if a closing takes more than 60 days they will no longer work with the respective MLO. Loans must close on time, every time, for an MLO to retain the agent's loyalty. Ninety percent of real estate agents say they expect loans to close on the designated date 95 percent of the time. And more than 80 percent expect closing dates to be within 30 days. In some markets (especially California), the loan contingency date may be even more important than the actual closing date (Exhibit 5).

Exhibit 5

Four of five realtors surveyed demand a 30-day close

How quickly should a plain vanilla loan close (days from rate lock to funding)?

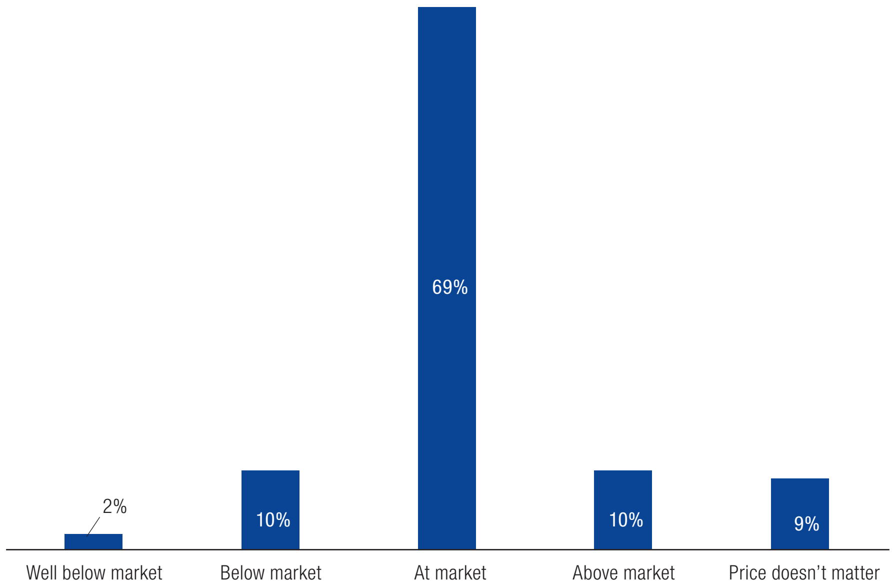


Source: McKinsey/Active Rain Realtor survey

Exhibit 6

Performance trumps price. Only 12% of realtors demand below-market pricing

How competitive does pricing need to be?



Source: McKinsey/Active Rain Realtor survey

Performance generally preempts price. Only 12 percent of agents prioritize their referrals to MLOs offering below-market rates. In fact, nearly 20 percent note that rates either do not matter or can be above market, provided that performance is superior (Exhibit 6).

Converting knowledge into closings

Acknowledging the influence of real estate agents in the purchase transaction and understanding their unique needs is an essential first step to attracting more prospects and closing more loans. There are a handful of tactics MLOs can implement quickly to build and solidify their agent relationships:

- Obtain borrowers' permission for the MLO and processor to confer directly with the real estate agent regarding the status of the application process. In most cases, agents' broad experience enables them to understand even better than the borrower those things that could become important issues in the transaction process.
- Always stay in close communication with borrowers and agents. Every two or three days is preferable—especially when there has been no status change. A lack of progress infuriates both agents and buyers, so each will appreciate news of progress, however small.
- Agents need leads, too. More than 60 percent of agents admit that an MLO who provides them with leads[3] will be placed on their MLO referral lists. Banks can even use their Web presence to stay in close contact with agents by providing leads and status updates on active applications. Lenders could also consider creating an agent-only online tool that provides more detail and real-time tracking than customers themselves might want.

[3] Subject to RESPA guidelines.

- Help agents stay informed about the market. More than 80 percent of agents would like loan officers to keep them updated on marketplace trends and new products.

Broader bank efforts to engage agents seldom pay off unless their MLOs are empowered to develop strong relationships with real estate agents.

It is important to note that real estate agents work primarily with MLOs, not banks; it is MLOs, after all, who typically return agents' calls. Broader bank efforts to engage agents seldom pay off unless their MLOs are empowered to develop strong relationships with real estate agents. Furthermore, for lenders, the loyalty of MLOs is crucial, and they can cultivate that loyalty by providing MLOs with the tools and marketing support they need to keep real estate agents satisfied and loyal to them. After all, if an MLO moves to another lender, the agent will likely follow.

Seven ways to build strong agent loyalty

McKinsey has identified seven approaches lenders can take to better support real estate agents and their customers and to build both agent loyalty and borrower satisfaction. The order in which they appear is that in which agents are most likely to notice change.

1. **Recruit selectively and train well.** Careful recruiting for MLOs can make an enormous difference to bottom-line performance. A stellar performer is frequently worth several mediocre ones. Human resource assessment tools for the sales profession can help, but sales abilities vary dramatically depending on what is being sold. A tool must enable sales managers to measure those attributes that distinguish high performing MLOs from their less productive peers. It is also vital to have a comprehensive and commonly understood profile of what constitutes MLO success.

2. **Locate loan officers strategically.** Geospatial mapping techniques can help lenders pinpoint where potential customers and real estate agent partners are located relative to their MLOs. Closely aligning MLO resources with current demand, and realigning them when markets shift, can generate significant performance improvement.

3. **Accept e-signatures.** Borrowers are often on the move and seldom near their computers when disclosures need to be signed. Enabling e-signatures from mobile devices and desktop computers can greatly expedite the return of critical disclosure documents to keep the mortgage process flowing smoothly. Similarly, enabling document submissions from common platforms, including uploads of mobile phone document photos, can be a major time-saver. The idea is to open those communications channels that customers and prospects use most, rather than the pathways most convenient to lenders.

4. **Provide credit decisions as soon as possible.** A homebuyer's greatest fear is that he or she will not qualify for the requested loan. Real estate agents also rest easier once their purchaser's loan request is approved. Good execution requires knowing which documents are most critical for approval, even if other documents might be required later. Rapid pre-qualifying and pre-approval help establish customers' bona fides. More than 80 percent of agents require prequalification letters *before* they'll

work with a homebuyer. More than 25 percent also insist that a credit check and some level of income and asset documentation be included. Underwriting customers and providing a lending commitment (subject to property appraisals, etc.) upfront creates a powerful bond with borrowers and their agents.

5. **Offer online status tracking.** Provide an online status tracking tool that is sufficiently detailed to be relevant, but not so detailed as to confuse. Most importantly, be absolutely certain that updating occurs in real time because inadvertently misleading agents and borrowers is worse than not updating them at all. All of the agents McKinsey surveyed say they require status updates, and 60 percent want them weekly. Separate online views for borrowers and real estate agents can show where a loan is in the processing pipeline and identify any items slowing progress. Having real-time transparency eliminates surprises and helps agents to be effective partners by prompting borrowers to quickly return required documents.

6. **Become fulfillment experts.** Although banks think of sales and fulfillment as separate functions, borrowers do not. Too often, poor prioritization and miscommunication in processing and underwriting cause delays and errors, which ultimately lead to missed closing dates, disgruntled agents and borrower misery. Frustrated borrowers might well take their business elsewhere. But, when you dissatisfy the real estate agent, you may lose an *entire pipeline* of loan seekers. Sales will actually benefit from rethinking the fulfillment process as realtor partners discover which lenders have the smoothest, most efficient processes.

7. **Automate simply.** Automation does not always need to be costly or complex. Simple automation can eliminate 80 percent of document problems before they occur. Automated checklists can be created on an office computer with common software that includes tools for automating document requests and tracking. One bank has developed a point-of-sale app that quickly identifies required loan documents. It also generates plain-English requests and conditions that tell borrowers and agents exactly which documents are needed, and why.

   Innovations like this are inexpensive and can be implemented quickly. Despite their simplicity, few lenders use these convenient tools, and instead rely on non-automated lists and other investor-provided, automated, underwriting engines that generate complex borrower requirements. Some of those requirements are only remotely applicable to the loan in question and rarely decipherable by borrowers asked to use them..

There is no single approach that guarantees lender success in the homebuyer marketplace.

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There is no single approach that guarantees lender success in the homebuyer marketplace. Lenders who survive and thrive will likely do so by layering best practices and building mortgage origination platforms that attract, deepen and retain strong relationships with those real estate agents they view as stakeholders and partners. Developing a marketplace advantage, then nurturing it, is an ongoing process—one that gradually builds agent trust and favor incrementally over time.

Given today's lower demand, higher conversion rates are critical. To achieve this, lenders need better quality leads, stronger sales skills—or both. This is what makes the real estate-agent relationship vitally important. Agents are frequently the first contact prospective homebuyers when seeking a new home.

Lenders will find the seven steps presented here of significant value in developing, or reinvigorating and maintaining their essential bonds with real estate agents in their target markets.

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