

Do it Yourself!

Credit Unions Don't Need Secondary Market Intermediaries

For anyone listening closely to it, the recent announcement that CUNA Mutual Group was selling its mortgage company subsidiary to PHH Corp. contained an important message: Nothing lasts forever.

Change is the only certainty in the mortgage business, and changes in interest rates, loan demand, or both will almost certainly make it attractive or essential for intermediaries to sell in the future mortgage servicing rights they may have every intention of holding today.

What is surprising is not that intermediaries would sell their servicing, but that credit unions would be surprised when they do. It's not as if they haven't seen this scenario before.

A little history is instructive. When the housing boom began to take shape a decade ago, credit unions started originating mortgages in earnest, recognizing accurately that members forced to go elsewhere for a mortgage would likely go elsewhere for other financial services, too. Entering a business they didn't know and weren't confident they could learn, credit unions responded eagerly to intermediaries who offered to do all of the secondary market heavy lifting for them.

Those offers were particularly appealing when they came from companies promoting their understanding of credit union operations and their sensitivity to the needs of credit unions and their members, especially when those companies offered to make the transaction invisible, so that members would think they were still dealing with their credit union rather than with a third party they didn't know.

A Crucial Link

Why did that matter? Because unlike secondary market intermediaries, credit unions view mortgage lending not just as a revenue stream, but also as a crucial link with their members. A home mortgage is the centerpiece of the financial services menu; lose the mortgage and you lose the opportunity to cross-sell home equity loans, automobile loans, personal loans, and a host of other products and services that form the foundation on which a primary financial relationship is built. Control the servicing on a mortgage and you control the member relationship.

And credit unions value their relationship with their members above all. They know credit union members

don't expect to be treated like bank customers. They certainly don't expect to wake up one day and discover that they must start sending their mortgage payment to an entity they don't know located hundreds or thousands of miles away. Credit union boards, sensitive to those concerns, will not enjoy fielding calls from members who can't get a response from the new servicer, or who are wondering what "crisis" forced the credit union suddenly to unload its loans.

Given those concerns, it is easy to understand why many credit unions would prefer to book their mortgages instead of selling them, but that is not a viable option. With interest rates rising and likely to remain on an upward trajectory for some time, long-term fixed rate mortgages will quickly become a dead – and potentially deadly – weight in credit union portfolios.

That creates an obvious dilemma. If credit unions have to sell their mortgage loans, which they do, but can't count on secondary market intermediaries to retain the servicing, which they clearly can't, what are they to do? The answer is clear: Skip the intermediaries and sell directly to Fannie Mae and Freddie Mac by becoming authorized seller-servicers in their own right.

A Viable Option

This is an option credit unions have not considered in the past, partly because they have assumed that Fannie and Freddie were interested in dealing only with the largest originators, and partly because the costs and complexity of the secondary market seemed to make the barriers to entry too high. Both factors have changed.

Recognizing that credit unions are world class loan originators, Fannie and Freddie are actively promoting seller-servicer relationships with them. On the credit union end, technology has simplified and streamlined secondary market procedures that used to be far more cumbersome, complex, and costly than they are today. Flexible seller-servicing arrangements accommodate smaller shops. If you need back-office help to manage rate risk or the origination, closing, or servicing details, there are companies, mine included, that can provide

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that support for you. And once credit unions make the move to go directly to the agencies, many more companies will position themselves to provide these support services.

Upside Down

For years, the intermediaries have encouraged credit unions to believe they could not operate in the secondary market without them, because they didn't want credit unions to consider the possibility that they might be able to handle this business on their own. The intermediaries were always a lot more interested in building their own business (acquiring servicing rights to loans with an excellent payment history) than in helping credit unions build theirs.

It's time to change this model. Third parties may have a place in the mortgage business of credit unions, but it is standing behind credit unions and supporting their operations, not getting in their way by providing services they don't need.

Credit unions don't need intermediaries to provide a bridge to the secondary market, but they do need to protect themselves and their member relationships, and the only



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way you can do that is by establishing seller-servicer links directly with the agencies and retaining control over the servicing of your loans. That way, you can decide when and to whom to sell the servicing if it becomes advisable or essential to do so, instead of putting that decision in the hands of intermediaries for whom the best interests of credit unions and their members will never be the primary concern.

Dealing directly with Fannie and Freddie is the right thing for credit unions because it is ultimately the best thing for credit union members. And most credit unions don't need any other motivation than that.