MARKETS

Homeowners Ditch Refinancings as Mortgage Rates Rise

Lenders turn to home-equity loans, adjustable-rate mortgages amid fears of falling home-purchase activity

A sign for a real-estate agency hangs outside a house in Uniondale, N.Y. An increase in interest rates has helped to reduce the number of borrowers who could benefit from a refinancing to about 37% from the end of last year, according to Black Knight Inc.
PHOTO: SHANNON STAPLETON/REUTERS

By Christina Rexrode
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Refinancings make up a smaller portion of the mortgage business than at any time in the past two decades, posing a challenge for lenders who already fear higher interest rates and climbing house prices could eventually depress purchase activity.

Last year, 37% of mortgage-origination volume was because of refinancings, according to industry research group Inside Mortgage Finance. That is the smallest proportion since 1995, and the number of refinancings is widely expected to shrink again this year. In 2012, refinancings were 72% of originations.

While purchase activity has climbed steadily from a post-financial-crisis nadir in 2011, growth in 2017 wasn't enough to offset a $366 billion decline in refinancing activity. The result: The overall mortgage market fell around 12%, to $1.8 trillion, according to Inside Mortgage Finance.

What's more, there are fewer homeowners eligible to refinance because of rising rates. The number of borrowers who could benefit from a refinancing is down about 37% from the end of last year, estimates Black Knight Inc., a mortgage-data and technology firm. At 2.67 million potential borrowers, this group is at its smallest since 2008.

"The market has just gotten so very competitive because every loan matters," said Ed Robinson, head of the mortgage business at Fifth Third Bancorp . He added that the bank is contacting homeowners who could be eligible for a refinancing in coming years to help maintain that business, and it is also instructing mortgage-loan officers to focus more on purchases.

Home-purchase activity has so far been holding up. Sales of previously owned homes in February rose 1.1% from a year earlier, countering worries that a downturn the previous month signaled a peak for the market.

Still, rising interest rates, a shortage of housing inventory and higher home prices are all long-term threats to purchase activity.

For refinancings, rising rates are a more immediate worry. Freddie Mac said last week that the average rate on a 30-year fixed-rate mortgage was 4.45%, up from 3.95% at the beginning of the year.

Increased mortgage rates can hamper refinancing activity because many homeowners have rates that are already lower than what lenders can now offer. In other cases, the higher rates cut into the savings a homeowner stands to reap by refinancing a mortgage.

A.J. Haverly was happy to refinance his Annapolis, Md., home in early 2016 to a lower rate. Recently, Mr. Haverly, 33 years old, looked into refinancing a rental home he owns, but rising rates dissuaded him.

"I keep my ears to the track, but rates have just been going up so there's no point in even calling somebody," Mr. Haverly said.

The Mortgage Bankers Association expects mortgage-purchase volume to grow about 5% in 2018 but refinancing volume to drop 27%. Refinance applications fell 5% in the week ended March 16 from the prior one, according to the group.

To drum up business, lenders are emphasizing home-equity lines of credit, which let borrowers tap their homes for cash through a new loan that doesn't affect the rate on their current mortgage. They are also pushing adjustable-rate mortgages, where initial rates are rising more slowly.

"I think we will see lenders focus on retaining their existing customers more fiercely," said Ben Graboske, an executive vice president at Black Knight.

Since around the beginning of 2017, Valley National Bancorp , based in Wayne, N.J., has transitioned its mortgage business to 40% refinancing from 90%, said Kevin Chittenden, who runs residential lending. The bank previously relied largely on attracting homeowners through its ads for low-cost refinancings, but has since engaged with outside sales reps who are focused on purchases.

> "Refi goes with the rates," Mr. Chittenden said. "So you definitely don't want to be too leveraged on refinancings."

For some lenders, though, that is easier said than done. Since the crisis, some lenders—particularly nonbanks—have gained prominence by using technology and aggressive marketing to offer refinancings. As well, refinancings can be operationally easier for a lender since there are no buyer-seller agreements and in many cases the lender already knows the homeowner.

Guy Cecala, chief executive of Inside Mortgage Finance, said he expects some smaller nonbank lenders to sell themselves by the end of the year because of the drop in the refinancing market and mortgage originations overall. Unlike banks, nonbank lenders typically don't rely on branches or ties to local agents, which are traditional tools for capturing mortgage purchases.

The waning of the refinancing boom also attracts a different type of homeowner than at the beginning. As mortgage rates go up, the average credit score of refinancings tends to go down, according to industry research.

That is partly because savvy borrowers are the ones who tend to take advantage of low interest rates first. Also, some borrowers who are refinancing now are doing so to get rid of their mortgage insurance: Home prices in many parts of the country are going up, meaning some homeowners are less leveraged even if they have paid down only a small portion of their mortgage.

Quicken Loans Inc. got about 70% of its mortgage-origination volume last year from refinancings, according to Inside Mortgage Finance—a higher proportion than any other large lender.

Quicken declined to comment on that estimate. Chief Executive Jay Farner said the company is still enjoying demand for both purchases and refinancings, including from homeowners whose decision to refinance is focused less on rates and more on consolidating debt or switching to a shorter-term loan.

But, he added, "You've got to be a little bit more strategic about how you market, versus what we saw lenders do in the last few years, which is, 'Hey, rates are low, you should do something now.' "

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