

“MORTGAGE FINANCING in MEXICO INCREASING FOR U.S. BUYERS”

By Mitch Creekmore, Stewart International



Owning a home has long been an American ideal we all strive to accomplish. Since World War II, home ownership has become a fundamental goal in our quest to achieve the “American dream.” Today, owning a *second* home has become a part of our “dream” for many Americans, and it has escalated to purchases in foreign jurisdictions. More than a million Americans have bought residences in Mexico over the past decade. Unlike the United States, for every 10 U.S. residences nine have mortgages, in Mexico, residential acquisitions by foreigners have principally been cash purchases. The reason is simple, a lack of available financing. However, this unfortunate fact has changed dramatically over the past 3 years in Mexico.

In order for mortgage markets to first emerge and then to grow, there are many primary requirements that must be in place. The U.S. mortgage system has become the benchmark model for other loan origination programs in the world. In the United States, the mortgage market can be explained as a “360°” process. First, financial institutions that originate loans must qualify prospective borrowers relative to their assets, debts and the requested loan amount. Subject to this assessment is the loan to value ratio and the required down payment. In essence, lenders arrive at a profile of the borrower’s overall credit worthiness and determine the acceptable parameters for a given mortgage. Once the mortgage has been originated, the loan will be pooled with other mortgages, and the loan portfolio will be rated according to the specific lender, borrower, financing terms, the asset itself, and the “age” of the mortgage. The rating that is placed on the loan pool will determine the “discount rate” for selling the portfolio. Selling the loan portfolio in the secondary mortgage market and offering mortgage backed securities to investors on Wall Street completes the cycle of liquidity in order to recapitalize primary mortgage lenders across the country. Though this explanation is extremely simplistic, it’s the basis for how the U.S. mortgage system thrives. In order for the system to thrive and moreover to survive, certain assurances and guarantees must be in place. Investors in mortgage backed securities don’t know local market conditions where the mortgages originate but they do know they will receive a certain yield on their investment, and the investment is guaranteed and secure. These assurances would include private mortgage insurance, title insurance, FHA, and VA guarantees, as well as a non-judicial foreclosure process, deeds of trust, and other standardized mortgage instruments.

Unlike the United States, the depth of the Mexican mortgage market is shallow, and Mexico does not have a secondary market for the creation of mortgage backed securities. The peso devaluation in 1994 further compounded the matter leading to a banking crisis of major proportion that reduced the liquidity of Mexican banks. Resources for new lines of credit largely disappeared until foreign banks entered and partnered with most of the Mexican banking institutions. There is still an estimated pent up demand for 6 million dwelling units in the country today due to the country’s inability to finance housing. However, U.S. buyers of

Mexican residential real estate don't face this same situation. There is an ever-growing awareness among U.S. purchasers that financing is available on Mexican properties. Several lenders such as Collateral International in Birmingham, M&I Bank in Phoenix, Silvergate Bank in San Diego, and ConfiCasa International in Houston, have expanded their Mexico lending programs for U.S. and Canadian buyers. In the last two years, GE Money, a subsidiary of GE Capital based in Mexico City, has emerged as well. With a cadre of more than 50 loan brokers all underwritten by WMC Mortgage in California according to GE Mexico lending parameters, companies like CS Financial, GS Mortgage, Finance North America, Platinum Capital, Mortgages in Mexico, Snell Real Estate, and many others can originate the loan application process for the benefit of their loan customers. Several other lenders will dot the financing landscape during 2006 with new mortgage products being offered from companies like GMAC/RFC, Textron Financial, Laredo National Bank, and the IMI Group of Phoenix. The various loan products have improved over time as well. Origination is generally 2-3 points with LTV's from 50-90 percent financed on 20-30 year amortization schedules. Interest rates vary from a 4 year fixed loan rate at 7.99 percent for GE Money loans to fixed rate loans of 20-30 years ranging from 7.25-9.0 percent interest depending on an individuals FICO score. There are even adjustable rate mortgages (ARM's) that some lenders offer. Make no mistake, in all cases, these loan products are based on a "full loan doc" underwriting criteria common with U.S. lending practices. It should also be noted that all of these lenders look to Mexican real estate as only collateral to the debt created and not to additional security or pledges in the United States.

There is a distinct and protective benefit that purchasers receive in financed operations. In order to finance Mexican residential properties, first and foremost, there **must be** a transfer and conveyance to a Mexican bank acting as trustee protocolized by the notario publico that establishes a recorded and renewable beneficiary interest for 50 years for the non-Mexican foreign buyer. The lender will be the first beneficiary of the bank trust with the borrower being the second beneficiary until the debt is extinguished. All residential transactions in Mexico (regardless of who the purchaser is) require payment of a transfer tax on the declared value of the operation, (which **should be** the purchase price and not what the seller or developer declares to minimize the capital gains tax) notary fees and recording costs. These expenditures are the norm in any Mexican property transfers, and they are not inexpensive by U.S. standards. Foreign buyers must also pay for the permit from the Ministry of Foreign Affairs, a bank trust appraisal fee, the first year trust fee to administer the fideicomiso, along with a trust registration fee, and a trust recordation fee. These expenditures are also customary and required. At the end of the day, the comparative expense of a cash transaction should run between 5-7 percent of the purchase price whereas financed acquisitions will average about 8-10 percent, the difference being the cost of the mortgage origination as previously mentioned. You, the buying public, must realize that real estate deals in Mexico are just more expensive than what we are accustomed to in the U.S.

Secondly, U.S. financial institutions, like those mentioned above, require a more detailed process to originate loans in Mexico. Possession of the property is not tantamount to ownership. Lenders must be assured, through a competent title search of the property and issuance of a Commitment for Title Insurance, that there is a complete chain of title for the respective residence. They want to know how the title is vested and that it is valid. Lenders are going to rely on the title company investigating the property that a subdivision has been approved and published or that a condominium development has a condominium regime filed of record. GE Money loans would be the exception to this rule, however. As of yet, GE does not require title insurance for their loans. Borrowers with GE should seek the protection of title services who can guarantee their beneficiary trust rights as established with title protection in the United States.

Escrow considerations and escrow agreements are common with U.S. lenders on Mexican transactions as well. As has been said before, Mexico is not the “Wild West” as many perceive. Lenders want a higher standard of assurance that the loans they originate are secure and the public deeds vesting the bank’s lien interest are valid and enforceable. This ultimately works to the benefit of the borrower. Anyone acquiring residential real estate can at least have the opportunity to check with U.S. based mortgage lenders on the availability of a Mexican home mortgage. Loan transactions for Mexico are originated and processed every month. With the emergence of the International Mortgage Lenders Association, who had their charter meeting with 65 business entities in Phoenix last March 24th, mortgage originations will become an even more common concept with U.S. purchasers. It is the goal and vision of the IMLA to create awareness and education of the mortgage procedures and products coupled with best practices initiatives for U.S. and Mexican consumers. We, Stewart International, are betting on the emergence of the Mexican mortgage market and the vision of the International Mortgage Lender’s Association. And, on **both sides** of the border!

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