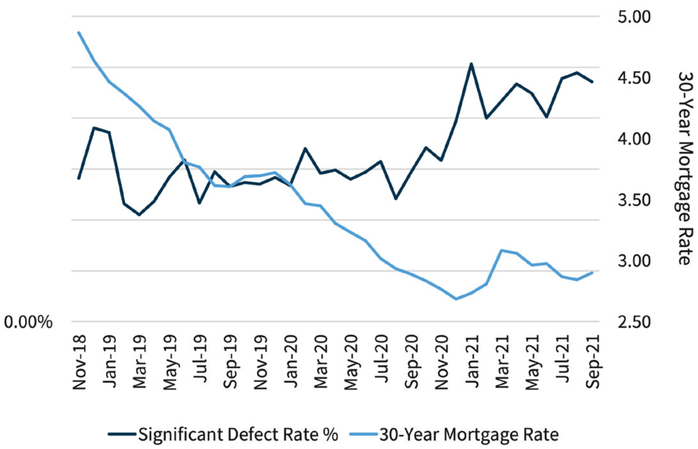
# Are You Prepared For a Market Shift?

In August 2024, the Fannie Mae Refinance Application-Level Index surged as homeowners applied for refinances at a pace not seen since August 2022. The increase, possibly due to the preceding drop of mortgage interest rates and the Federal Reserve's cut in the federal funds rate, could be indicative of an upcoming increase in refinance activity.

Quality control teams should be aware of the potential for change. While quality control is critical regardless of the interest rate environment, history has shown that transitions between different market cycles can have impacts on defect rates across the industry.

For example, from November 2018 through September 2021, the average 30-year mortgage rate dropped from 4.87% down to a historically low 2.90% before it started a slow than sharp move upward. The significant defect rate in Fannie Mae's loan quality random reviews moved upward as interest rates decreased:




QC teams should proactively prepare for shifts in volume and loan types by adding component reviews in prefunding QC, moving QC reviewers from post-closing to prefunding and action planning based on the review results.

Expand component reviews that focus on refinance transactions. Subjects for component reviews can include, among many others, excluded liabilities, credit inquiries, self-employment documentation, self-employment income, and DTIs with smaller margins of error.

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Even in a changing interest rate environment, some of the significant defects cited by Fannie Mae stay relatively consistent. Continue to strengthen risk controls in areas including self-employment calculations and self-employment documentation as well as borrower employment requirements. Reinforce vigilance on undisclosed liabilities and calibrate discretionary reviews in both prefunding and post-closing based on the types of loans you are originating.

Be aware of defects cited during the last refinance boom to make sure controls are in place or need to be enhanced to prevent those defects from recurring as refinance activity increases.

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