Impact of Post-Crisis Regulations on Market Dynamics, Lending, and Balance Sheets

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Outline

Mortgage Origination Activity
• In the aftermath of the financial crisis there has been a decline in purchase activity and a contraction in credit availability
• A major reshaping of the mortgage industry has also occurred, including a huge growth of non-bank originators and lower concentration
• Most of this is due to mortgage-specific issues, and not increased bank regulation

Private-Label Mortgage Securitization Activity
• Private label mortgage securitization activity is low; other asset securitization activity much more robust
• Risk retention is not the issue; the QRM rules have been neutered
• The issuer paid rating agency model did not change
• 2 issues, (1) it is not economic to securitize and (2) there is a lack of investor trust
• Other asset classes did not experience as sharp a rise in delinquencies
• The institutional framework for other assets did not change; they did change for mortgages (extending timelines, mortgage modification activity)
• My prediction—MBS securitization is not coming back for lower quality mortgages, private pools of money will hold the assets in whole loan form.

Agency MBS Activity
• Post crisis, there is not much change in dealer agency MBS net positions, repo activity is down, and transactions volume is down
• Agency MBS transactions volume is still quite high, especially relative to corporates
• Other non-regulatory reasons agency MBS transactions volume is down: decreased refinancing activity and decreased mobility
Home sales and new purchase mortgage volume

Sources: US Census Bureau, National Association of Realtors, HMDA and Urban Institute.
Note: Purchase mortgage counts derived from HMDA data. First liens for 2001-2003 are Urban Institute estimates.
Cash Sales Share

Percent of all home sales

Source: CoreLogic.
FICO score distribution of new borrowers

Source: Urban Institute calculations from HMDA and CoreLogic data.
## Quantifying the missing loans: 1.2 million in 2013, 4 million 2009-2013

<table>
<thead>
<tr>
<th>Loan category</th>
<th>2001</th>
<th>2013</th>
<th>2001, scaled to HMDA</th>
<th>2013, scaled to HMDA</th>
<th>Percent decline</th>
<th>2013, assuming 8.9% decline from 2001</th>
<th>Missing loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>CL-HMDA merged loans, &lt;660</td>
<td>720,614</td>
<td>163,692</td>
<td>1,310,317</td>
<td>317,474</td>
<td>75.8%</td>
<td>1,193,697</td>
<td>876,222</td>
</tr>
<tr>
<td>CL-HMDA merged loans, 660-720</td>
<td>723,009</td>
<td>427,262</td>
<td>1,314,672</td>
<td>828,657</td>
<td>37.0%</td>
<td>1,197,664</td>
<td>369,007</td>
</tr>
<tr>
<td>CL-HMDA merged loans, &gt;720</td>
<td>1,114,387</td>
<td>951,802</td>
<td>2,026,327</td>
<td>1,845,980</td>
<td>8.9%</td>
<td>1,845,980</td>
<td>0</td>
</tr>
<tr>
<td>CL-HMDA merged loans, Total</td>
<td>2,558,010</td>
<td>1,542,756</td>
<td>4,651,317</td>
<td>2,992,112</td>
<td>35.7%</td>
<td>4,237,341</td>
<td>1,245,229</td>
</tr>
<tr>
<td>HMDA alone total</td>
<td>4,651,317</td>
<td>2,992,112</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>HMDA alone to CL-HMDA merged ratio</td>
<td>1.82</td>
<td>1.94</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: Urban Institute calculations from HMDA and CoreLogic data.
HFPC Credit Availability Index shows credit is very tight

Percent

Source: CoreLogic, HMDA and Urban Institute calculations.
Increase in Ginnie Mae non-bank servicing share

FY 2010: $389 billion in SF issuance
- Depository, 82%
- Non-depository, 18%

FY 2014: $277 billion in SF issuance
- Depository, 49%
- Non-depository, 51%

Source: Ginnie Mae and Urban Institute.
Much less concentration in mortgage origination

Top issuers' Market Share: FHA and GSE loans

<table>
<thead>
<tr>
<th>Year</th>
<th>FHA Top 5</th>
<th>FHA Top 10</th>
<th>FHA Top 25</th>
<th>FHA 25th issuer</th>
<th>GSE Top 5</th>
<th>GSE Top 10</th>
<th>GSE Top 25</th>
<th>GSE 25th issuer</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>71.9</td>
<td>83.4</td>
<td>93.4</td>
<td>0.3</td>
<td>60.9</td>
<td>73.6</td>
<td>83.5</td>
<td>0.3</td>
</tr>
<tr>
<td>2012</td>
<td>63.9</td>
<td>74.0</td>
<td>87.2</td>
<td>0.6</td>
<td>46.4</td>
<td>59.0</td>
<td>70.7</td>
<td>0.5</td>
</tr>
<tr>
<td>2013</td>
<td>53.1</td>
<td>66.3</td>
<td>82.3</td>
<td>0.6</td>
<td>42.3</td>
<td>53.5</td>
<td>67.7</td>
<td>0.5</td>
</tr>
<tr>
<td>2014</td>
<td>40.1</td>
<td>55.8</td>
<td>75.1</td>
<td>0.9</td>
<td>32.6</td>
<td>44.7</td>
<td>61.6</td>
<td>0.7</td>
</tr>
<tr>
<td>2015 Q1</td>
<td>37.6</td>
<td>50.6</td>
<td>73.8</td>
<td>1.1</td>
<td>32.4</td>
<td>43.2</td>
<td>60.5</td>
<td>0.7</td>
</tr>
</tbody>
</table>

Sources: Inside Mortgage Finance and Urban Institute calculations from eMBS data.

Note: Market share was calculated using total loan balance.
Qualified Mortgage (QM) rules (effective January 10, 2014)

**Non-QM:**
- Negative Amortization Loans
- Interest Only Loans
- Loans with Balloon Payments (except for small creditors serving rural areas)
- Loans with terms exceeding 30 years
- Loans with no verification of income and no verification of assets
- Loans with upfront fees >3%, higher fees are permitted for smaller loans (up to 2 bona fide discount points are exempt):

<table>
<thead>
<tr>
<th>Loan Amount</th>
<th>Cap</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100,000 or more</td>
<td>3%</td>
</tr>
<tr>
<td>$60,000 to $99,999</td>
<td>$3,000</td>
</tr>
<tr>
<td>$20,000 to $59,999</td>
<td>5%</td>
</tr>
<tr>
<td>$12,500 to $19,999</td>
<td>$1,000</td>
</tr>
<tr>
<td>Less than $12,500</td>
<td>8%</td>
</tr>
</tbody>
</table>

- Loans > 43% back end Debt to Income Ratio and ineligible for agency execution

**QM:**
Loans must have standardized features including regular periodic payments that are substantially equal, except for the payment changes on an Adjustable Rate Mortgage. Upfront points can not be more than 3%. Loan must have back-end Debt To Income Ratio ≤43% or be eligible for agency execution.

**Safe Harbor:**
Mortgage Rate ≤1.5% above the prime mortgage rate

**Rebuttable Presumption:**
Mortgage Rate >1.5% above the prime mortgage rate

How do you rebut a rebuttable presumption?
*By showing a borrower has insufficient residual income. Insufficient vs. sufficient residual income is never defined*

Sources: Amherst Securities and CFPB.
Effect of QM has been muted

Share of loans under $100,000

Share of Loans with DTI>43

Sources: eMBS, CoreLogic Servicing, and Urban Institute calculations.
Mortgages are more time-consuming to underwrite

Retail applications per underwriter per month

(applications per retail underwriter per month)

Sources: Peer Group Program conducted by Mortgage Bankers Association and STRATMOR Group.
Servicing costs per loan are way up, productivity down

<table>
<thead>
<tr>
<th>Year</th>
<th>Performing</th>
<th>Non-performing</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>$482</td>
<td>$59</td>
</tr>
<tr>
<td>2009</td>
<td>$703</td>
<td>$76</td>
</tr>
<tr>
<td>2010</td>
<td>$896</td>
<td>$90</td>
</tr>
<tr>
<td>2011</td>
<td>$1,362</td>
<td>$96</td>
</tr>
<tr>
<td>2012</td>
<td>$2,009</td>
<td>$114</td>
</tr>
<tr>
<td>2013</td>
<td>$2,357</td>
<td>$114</td>
</tr>
<tr>
<td>2014</td>
<td>$1,949</td>
<td>$158</td>
</tr>
</tbody>
</table>


Sources: Mortgage Bankers Association and Urban Institute calculations.
Actions to resolve overlays and open the credit box

FHA
• FHA quality assurance program
  • New FHA guidebook, putting together 900 mortgagee letters (partial draft completed)
  • New method for evaluating underwriting defects and severity
  • Supplemental performance metric to mitigate negative impact of Compare Ratio
• Annual mortgage insurance premium reduction

FHFA
• Relaxed pay rules for rep and warrant sunsets
• Provide additional clarity concerning GSE rep and warrants framework
  • Originations (better definition of life of loan reps)
  • Servicing, remedies for poor performance
• 97 LTV lending reinstated at GSEs
First Lien Origination Share

Sources: Inside Mortgage Finance and Urban Institute.
Non-Agency MBS Issuance

($ billions)


Re-REMICs and other $8,369
Scratch and dent $8,971
Alt A $0
Subprime $0
Prime $4,600

Sources: Inside Mortgage Finance and Urban Institute.
Securitization of non-mortgage asset classes

Securitization of non-mortgage asset classes

$ billions

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Pct change from 2001 to 2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Auto</td>
<td>14.4%</td>
</tr>
<tr>
<td>Credit Card</td>
<td>-22.9%</td>
</tr>
<tr>
<td>Student</td>
<td>-5.3%</td>
</tr>
<tr>
<td>High-yield CLO</td>
<td>155.8%</td>
</tr>
<tr>
<td>CMBS</td>
<td>-17.7%</td>
</tr>
<tr>
<td>Non-agency MBS</td>
<td>-84.2%</td>
</tr>
</tbody>
</table>

Lack of investor trust: some issues solved, some not

Issues that have been corrected
• Structural flaws in pre-crisis securitizations—cash flows were released to the subordinate bonds early in the life of the deal, providing inadequate protection of the AAAs if loses are incurred later in the life of the deal
• Inadequate information at origination—this has been corrected, Project ReStart suggested 157 fields most deals have more.
• Due diligence was not taken seriously—this has been corrected.

Remaining issues
• Lack of standardization
• Reps and warranties: need mechanisms for detection and enforcement
• Who is looking for investor interests?
  - Should there be an independent collateral manager?
  - Should that party have a fiduciary responsibility?
• Lack of disclosure on servicing practices
  - How exactly are the loans being modified?
  - Does the servicer own the second lien?
  - How much is being charged for property preservation?
  - Does the servicer own the lawn mowing service?
  - Who is monitoring the servicer?
Delinquency rates by loan product

Documenting the severity of the crisis

Cumulative Modifications and Liquidations

Sources: Hope Now Reports and Urban Institute.
Note: Liquidations includes both foreclosure sales and short sales.
REO timelines by date of liquidation

Sources: Black Knight McDash Servicing Data, Federal Reserve Bank of Philadelphia RADAR Group Calculations
Agency MBS dealer activity: net positions unchanged, repos down

Sources: Federal Reserve Bank of New York and Urban Institute calculations.
Note: A five-week moving average of net positions was computed for this figure.
US Bond Markets Average Daily Trading Volume

$ billions

Treasury, $506.6
Agency MBS, $209.9
Corporate, $23.1

Sources: SIFMA and Urban Institute calculations.
Agency MBS and Corporate markets are similar in size

Outstanding US Bond Market Debt

Issuance in the US Bond Market

Sources: SIFMA, Inside Mortgage Finance, eMBS and Urban Institute calculations.
Non-regulatory reason for decline in transactions volume: conventional prepayments less responsive to interest rates

Conventional S-Curves

Note: 0-48 WALA
Source: Fannie Mae, Freddie Mac, 1010data, Amherst Pierpont Securities
Non-regulatory reason for decline in transactions volume: Mobility has been declining for decades

Sources: U.S. Bureau of the Census, CPS Historical Geographical Mobility Tables and Urban Institute.