Government Credit Pricing

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Federal Reserve Board

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The analysis and conclusions set forth are those of the author and do not indicate concurrence by other members of the research staff or the Board of Governors

Introduction

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  - Differences in appetite for credit risk between private sector and GSEs : are G-fees competitive?
  - Liquidity differences (eligibility to trade in the TBA market)

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- Explore rate spreads between Jumbo and Conforming loans, which capture:
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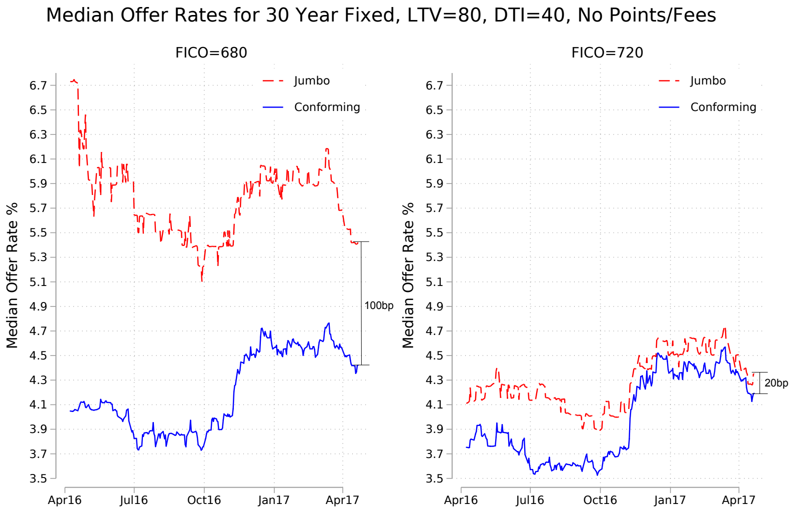
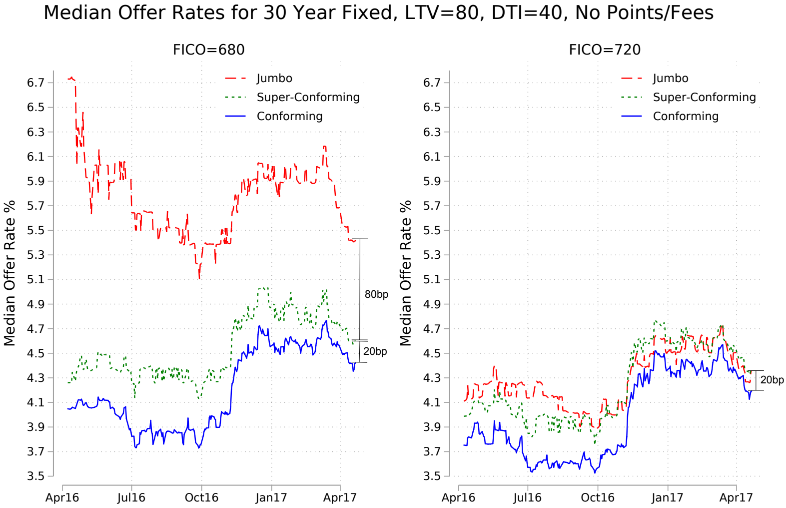
  - Liquidity differences (eligibility to trade in the TBA market)
- Use new dataset on daily mortgage rate offers
  - Optimal Blue Insight allows mortgage banks to compare pricing with their peers
  - We observe rates that would actually be paid by borrowers

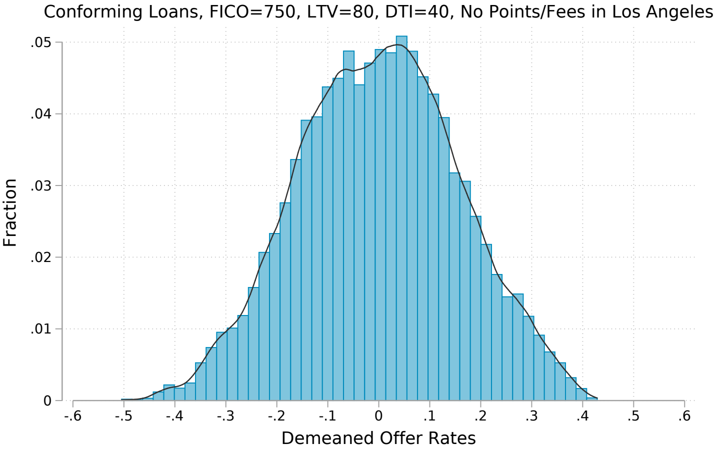


- Total benefit to borrowers from GSE mortgages :
  - ≈100bp for non-prime borrowers, ≈20bp for prime borrowers



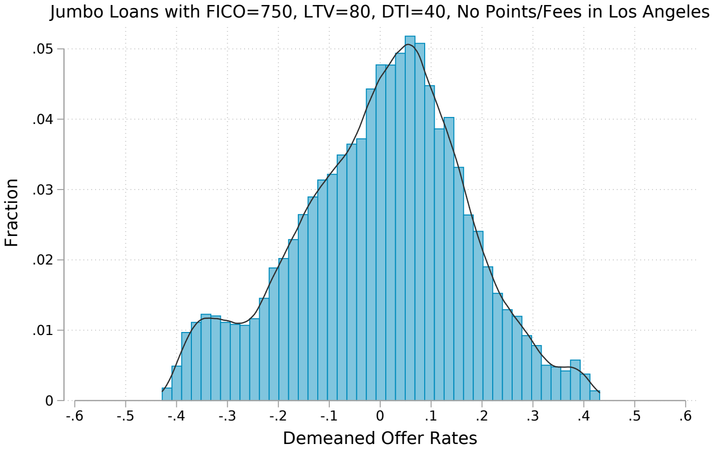
- Likely benefit due to TBA market liquidity ≈20bp
- Credit risk subsidy:
    - ≈80bp for non-prime borrowers, ≈0bp for prime borrowers

Wide distribution in offer rates for conforming loans



- Average rates mask large heterogeneity in offers for the same borrower in the same day in the same market

Wide distribution in offer rates for jumbo loans



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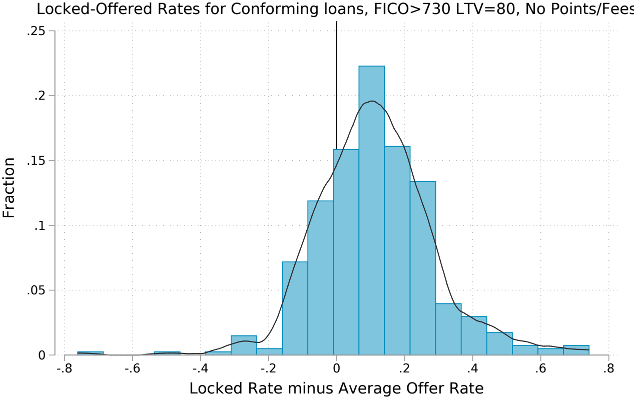
Do borrowers pick low rates from the offer distribution?



- Merged daily data on rate locks with offer rates:
  - on average conforming borrowers pay rates that are 17bp higher than the median offered rate.

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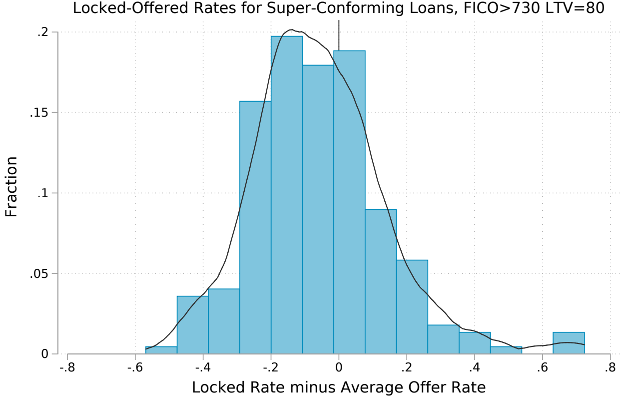

- Merged daily data on rate locks with offer rates:
  - on average super-conforming borrowers pay rates that are 2bp lower than the median offered rate.

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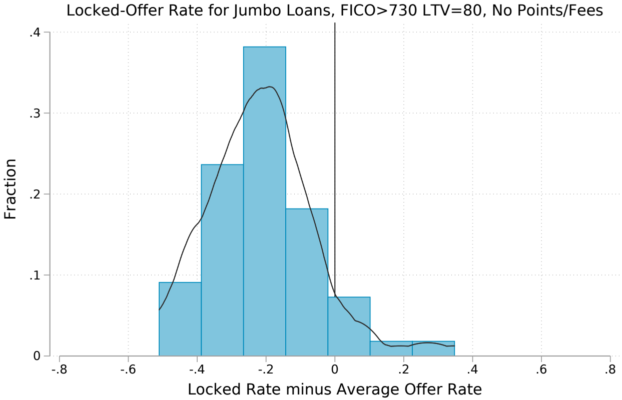
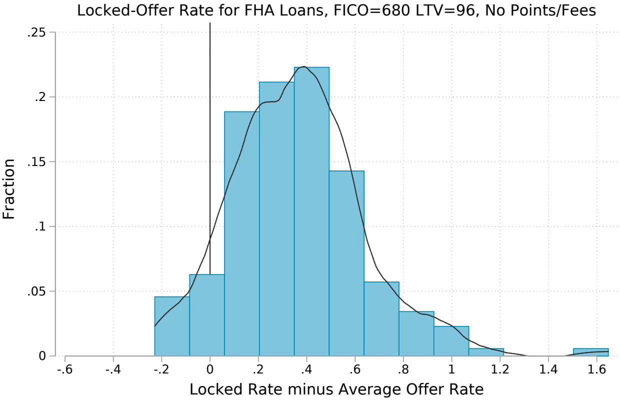


- Merged daily data on rate locks with offer rates:
  - on average Jumbo borrowers pay rates that are 24bp lower than the median offered rate.

Do borrowers pick low rates from the offer distribution?



- Merged daily data on rate locks with offer rates:
  - on average FHA borrowers pay rates that are 38bp higher than the median offered rate.

Conclusion

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  - Better rate choices by jumbo borrowers likely explain the reported negative jumbo-conforming spread

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  - Lack of rate shopping washes out a good part of the subsidies for GSE and FHA market
  - Better rate choices by jumbo borrowers likely explain the reported negative jumbo-conforming spread
- Policies that mitigate this problem would allow GSEs and FHA to increase g-fees further without affecting affordability:
  - Include info on current rates in the Lock agreement
  - Don't guarantee mortgages with too high of a spread etc.