

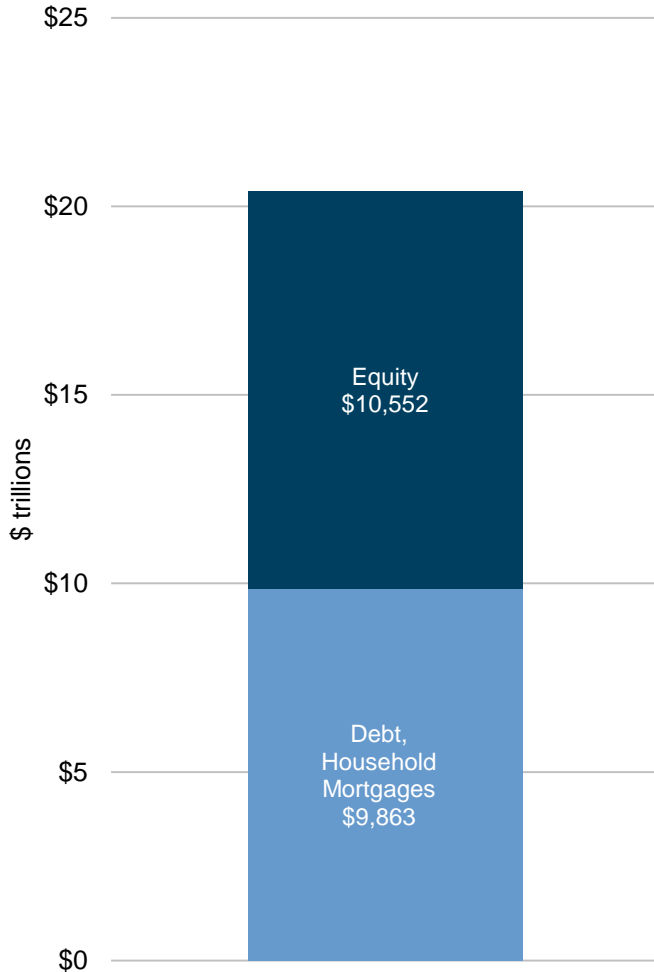
The Housing Finance Market: With and Without GSE Reform

Laurie Goodman
Center Director
Housing Finance Policy Center
Urban Institute

The Hoyt Group
Weimer School of Advanced Studies in
Real Estate and Land Economics
Palm Beach County, FL
May 17, 2014

Value of the US Housing Market

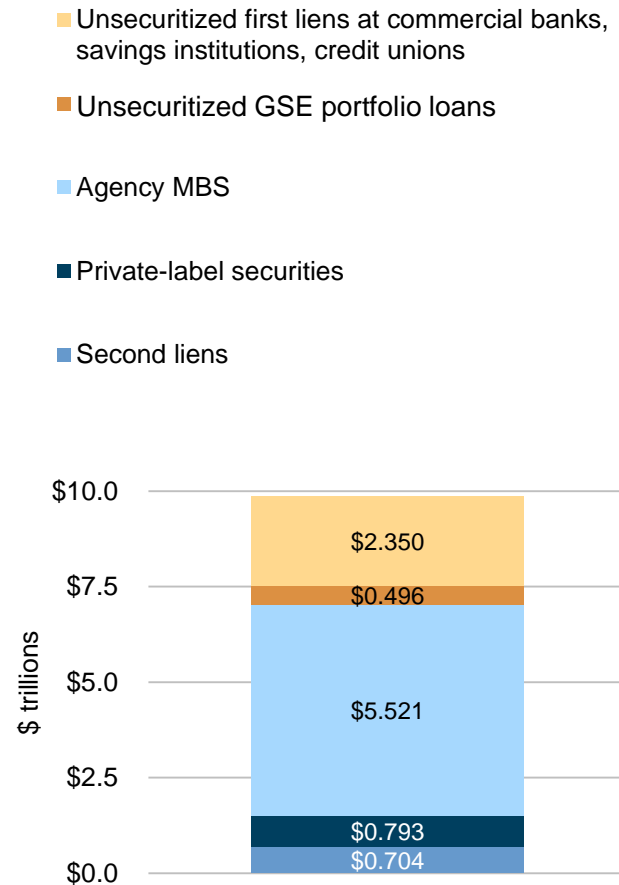
as of Q4 2013



Sources: Federal Reserve Flow of Funds and Urban Institute.

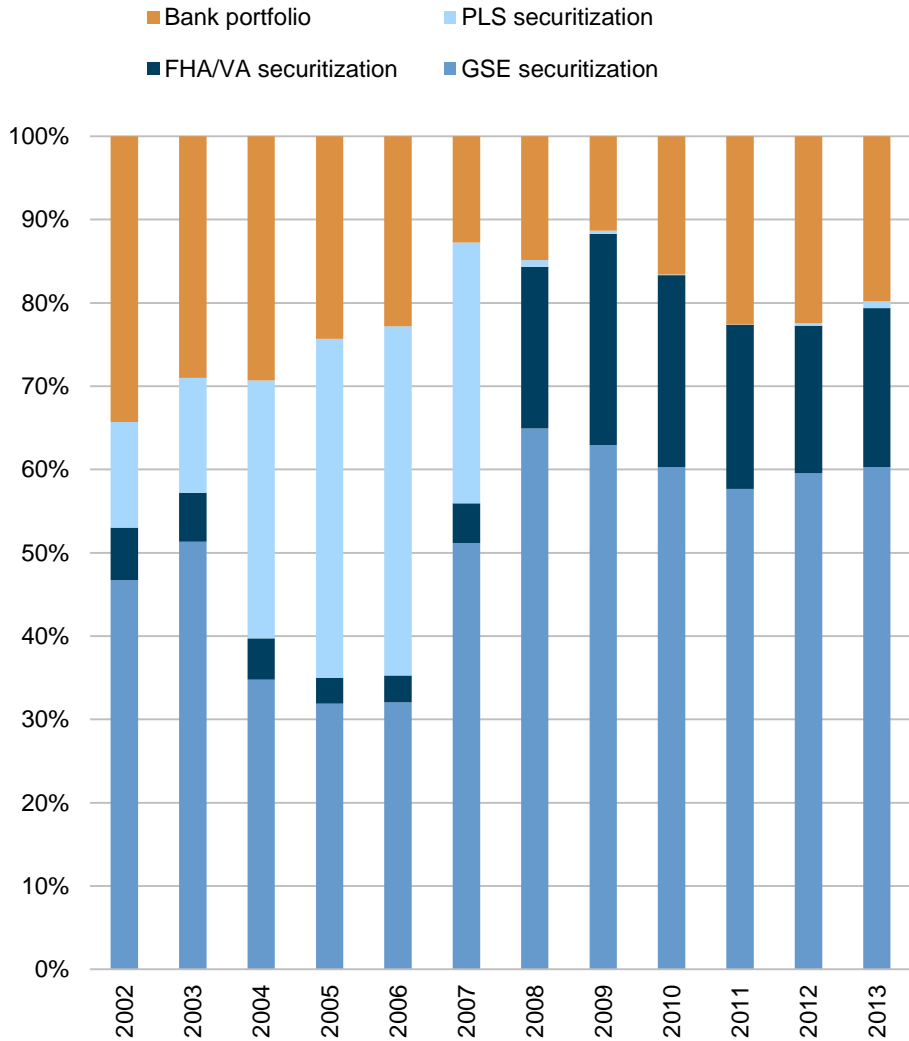
Size of the US Residential Mortgage Market

as of Q4 2013



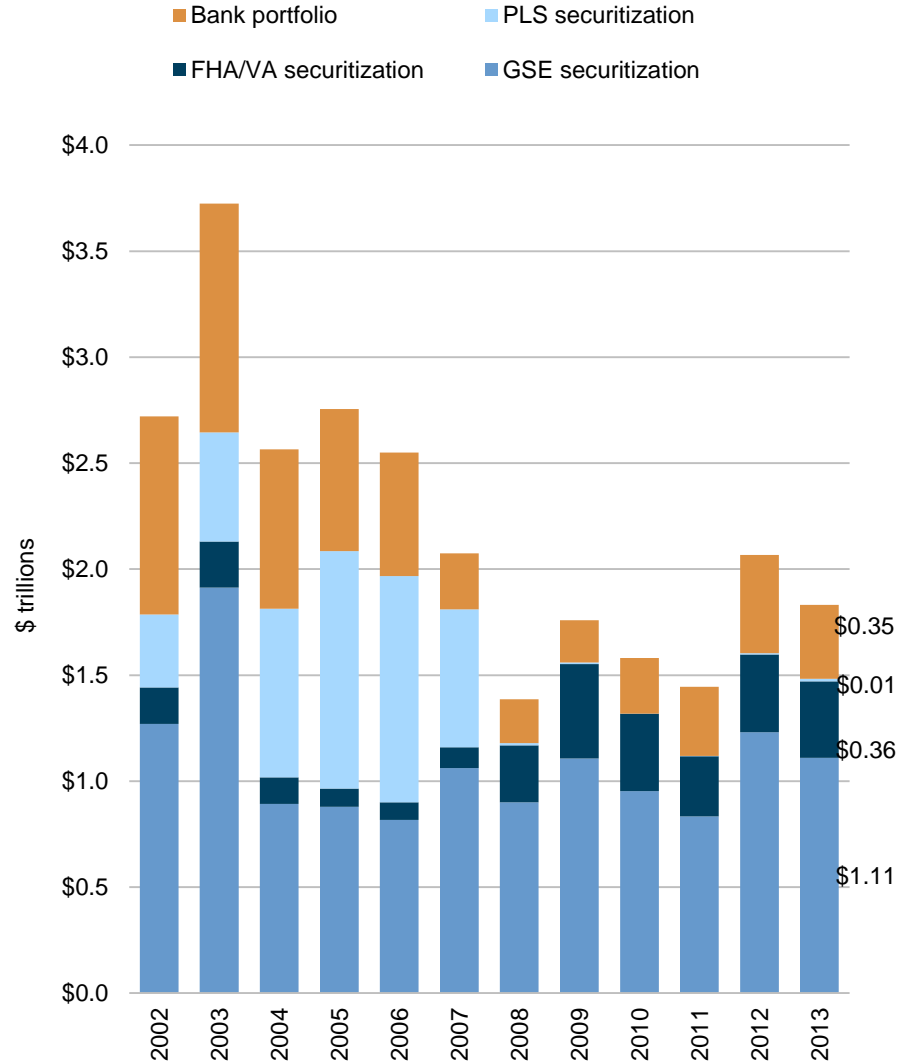
Sources: Federal Reserve Flow of Funds, Fannie Mae, Freddie Mac and Urban Institute.

First Lien Origination Share



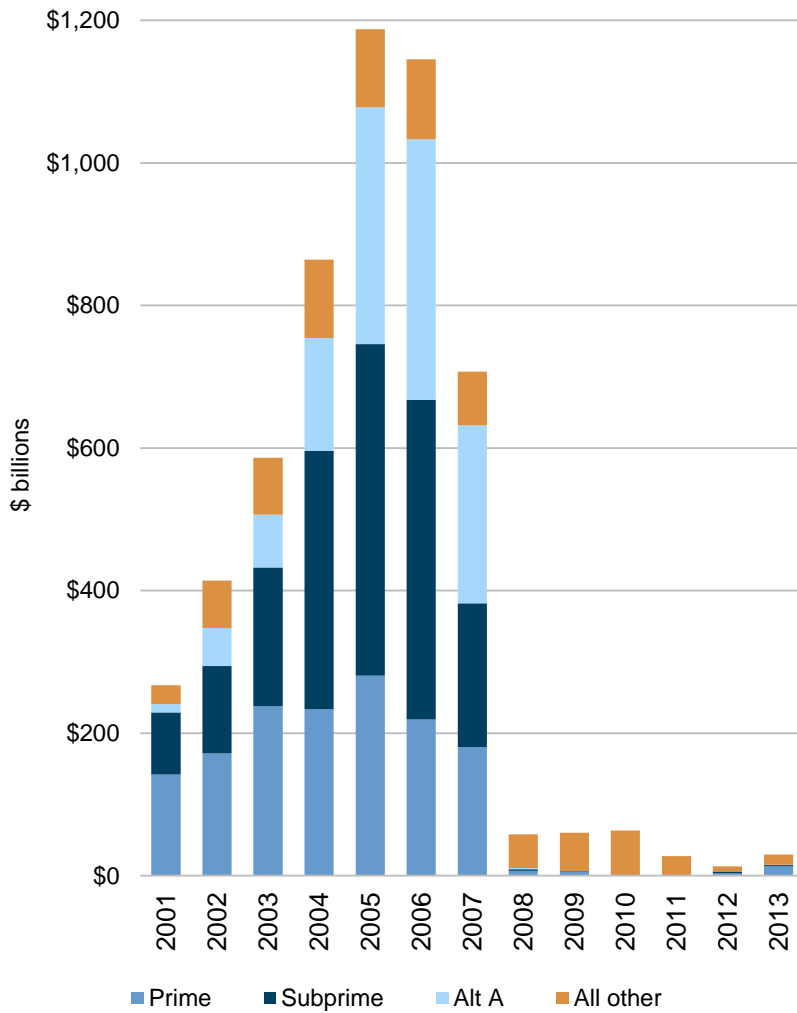
Sources: Inside Mortgage Finance and Urban Institute.

First Lien Origination Volume



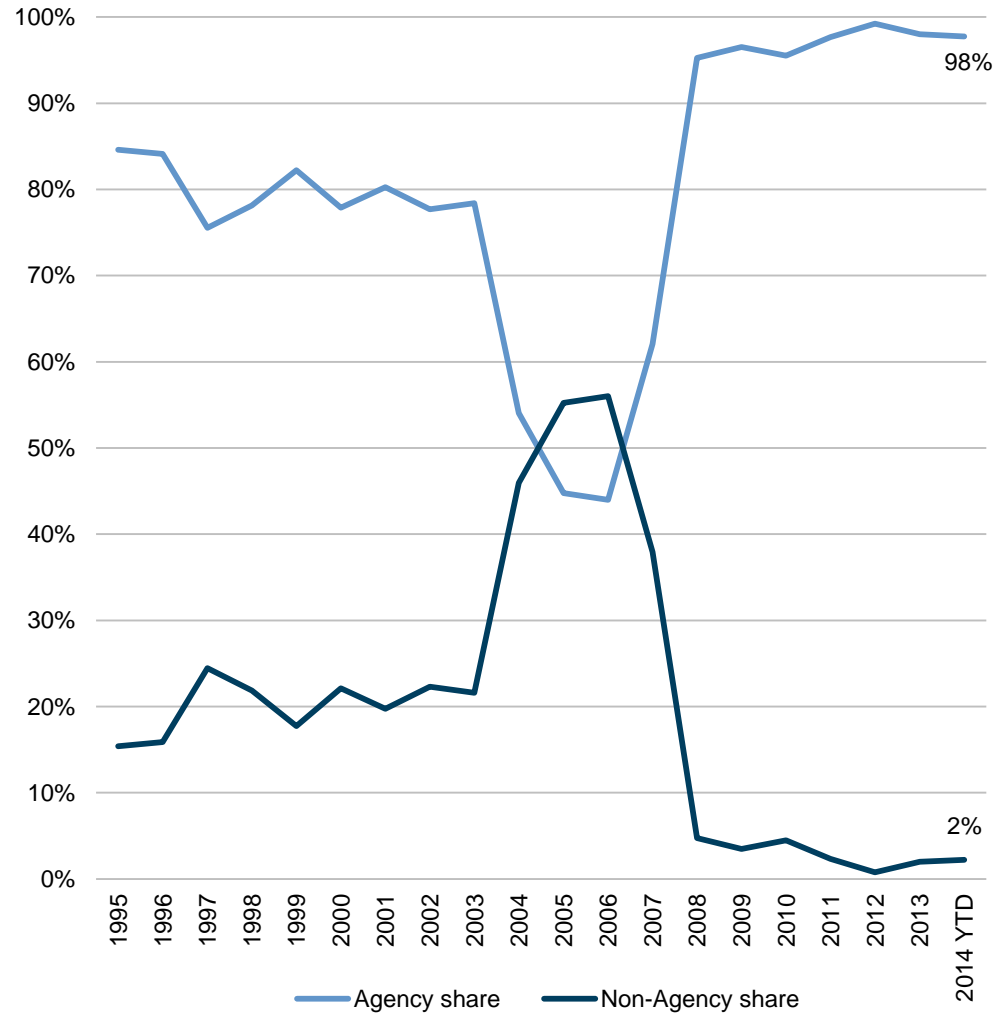
Sources: Inside Mortgage Finance and

Non-Agency MBS Issuance



Sources: Inside Mortgage Finance and Urban Institute

Agency/Non-Agency Share of Residential MBS Issuance



Sources: Inside Mortgage Finance and Urban Institute.

Note: Year-to-date figures as of March 2014.

Pricing

Bank Portfolio Execution

Hold on a bank balance sheet

Coupon on the mortgage	4.5
– Credit costs	0.10
– Option costs	0.55
– Servicing costs	0.05
– Annualized origination costs	0.50
– Cost of funds	2.1505
– Cost of capital	0.9165
Total proceeds	0.233

GSE Execution

Securitize with a government guarantee

	Present
Coupon on the mortgage	4.5
– Note rate on the mortgage	3.5
– Guarantee fee	0.5
= Servicing proceeds	0.5
Agency MBS price minus par	1.5
+ (= Annualized gain on sale)	0.33
– Servicing costs	0.05
– Annualized origination costs	0.5
– Capital charge on MSR	0.03
= Total proceeds	0.25

PLS Execution

Securitize without a government guarantee

Coupon on the mortgage	4.5
– Cost of senior bond	3.6
– Cost of subordinated bond	0.54
– Servicing costs	0.05
– Annualized origination costs	0.5
– Capital charge on MSR	0.04
Total proceeds	-0.23

Structure, Due Diligence, and Information at Origination have Improved Substantially in Securitization 2.0

- Structural changes help ensure that cash flows are not released to the subordinate bonds early in the life of the deal, providing inadequate protection to the AAAs if losses are incurred later in the life of the deal
- Structural changes:
 - The introduction of a fixed subordination floor, expressed as a % of original balance
 - The so-called 2x test is eliminated (if subordination reached 2x is initial level, the subs would be paid pro rata)
- Improvements in due diligence:
 - 100% sample of unseasoned originators, heavy sample of seasoned originators rather than a small sample as in Securitization 1.0
 - Will there be a race of the bottom in due diligence? Many are concerned
- Information at Origination:
 - 157 fields suggested by Project ReStart. Most deals provide more.
 - Only full documentation loans

Remaining Issues

- Lack of standardization
- Who is looking for investor interests?
 - Who should be?
 - Should trustees or servicers have a fiduciary responsibility to investors?
 - Should there be an independent collateral manager?
- Reps and warranties: need mechanisms for detection and enforcement.
- 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?
- SFIG Project RMBS 3.0 Workstreams
 - Reps and warranties/enforcement
 - Due diligence/loan data/disclosure
 - Trustee responsibilities/bondholder communication

GSE Reform: Agreement on principals, not on implementation

Widespread agreement on big issues

- preserve 30-year fixed rate mortgage
- preserve TBA market
- private capital takes first loss
- catastrophic government guarantee
- small and large lenders can access market

Disagreement on Implementation

1. Form, amount of private capital
 - a) guarantor only, or guarantor + capital markets execution
 - b) how much?
2. What does new structure look like?
 - a) new government agency (FMIC in CW and JC) is the securitizer
 - b) who is the issuer: the originator (as in GNMA securities), the aggregator, the guarantor, or the platform (as in GSE securities) ?
 - c) who is the aggregator: the guarantor, the platform, the originator, or the FHLBs?
3. Is the Mortgage Insurance Function separate from the guarantor functions?
4. What does transition look like? How do you go from a duopoly to more guarantors? Do Fannie and Freddie continue to operate as guarantors alongside new entrants?
5. How do you handle affordable housing? Goals, incentive fee, or another option? How is it structured?

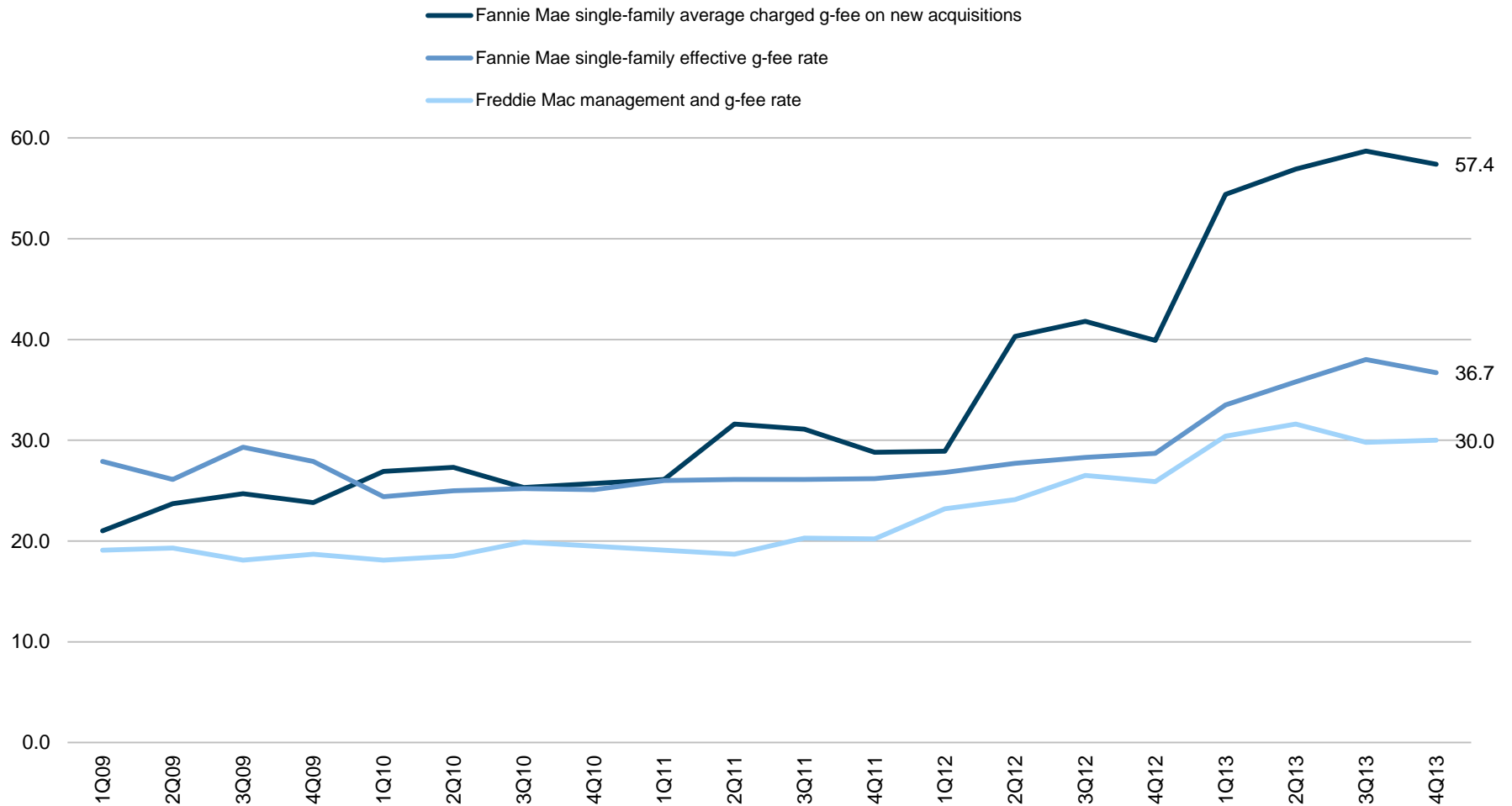
Why GSE Reform Is Unlikely Before 2017

- There is no sense of urgency: GSEs are profitable, current system is functioning.
- Higher legislative priorities.
- No easy answers as to what a new housing finance system should look like.
- Bipartisan action requires compromise, and some believe they have more to lose than to gain by compromising in this arena.

Bringing Private Capital Back: Administrative Solutions

- Crowd in private capital: contract the GSE footprint
 - Higher guarantee fees
 - Lower loan limits
- Bring in private capital: no contraction in GSE footprint
 - Back-end risk sharing (capital market and reinsurance deals)
 - Front-end risk sharing (MBA proposal)
- Challenge-- opening the credit box
 - Overlays are a huge issue

Effective Guarantee Fees



Sources: Fannie Mae, Freddie Mae and Urban Institute.

Note: Freddie only reports the effective g-fee on the entire book of business.

Fannie Mae Risk-Sharing Transactions

- Total reference pool sizes for CAS deals: \$56 billion in 2 deals
- Total Fannie Mae S.F. outstanding: \$2585 billion
- % partially covered: 2.1%

Class	Amount (\$ millions)	Tranche Thickness (%)	CE (%)	Rating	Initial Spread (bps)
Fannie Mae: Connecticut Avenue Securities (CAS) 2013-C01 October 24, 2013					
A-H	\$25,953.7	97	3	NR	-
M-1, M-1H, Total	\$337.5, \$23.7, \$361.2	1.26, 0.09, 1.35	1.65	F: BBB-sf	200
M-2, M-2H, Total	\$337.5, \$23.7, \$361.2	1.26, 0.09, 1.35	0.30	NR	525
B-H	\$80.3	0.30	0	NR	-
Reference Pool Size	\$26,756.4	100			
Fannie Mae: CAS 2014-C01 January 14, 2014					
A-H	\$28.4	97	3	NR	-
M-1, M-1H, Total	\$375, \$20.7, \$395.7	1.28, 0.07, 1.35	1.65	F: BBB-sf; M: Baa2	160
M-2, M-2H, Total	\$375, \$20.7, \$395.7	1.28, 0.07, 1.35	0.30	NR	440
B-H	\$87.9	0.30	0	NR	-
Reference Pool Size	\$29,308.7	100			

Sources: Fannie Mae and Urban Institute.

Note: Classes A-H, M-1H, M-2H, and B-H are reference tranches only. These classes are not issued or sold. The risk is retained by Fannie Mae and Freddie Mac. "CE" = credit enhancement. Under "Ratings," "F" = Fitch, "M" = Moody's, and "K" = "Kroll Bond Ratings."

Freddie Mac Risk-Sharing Transactions

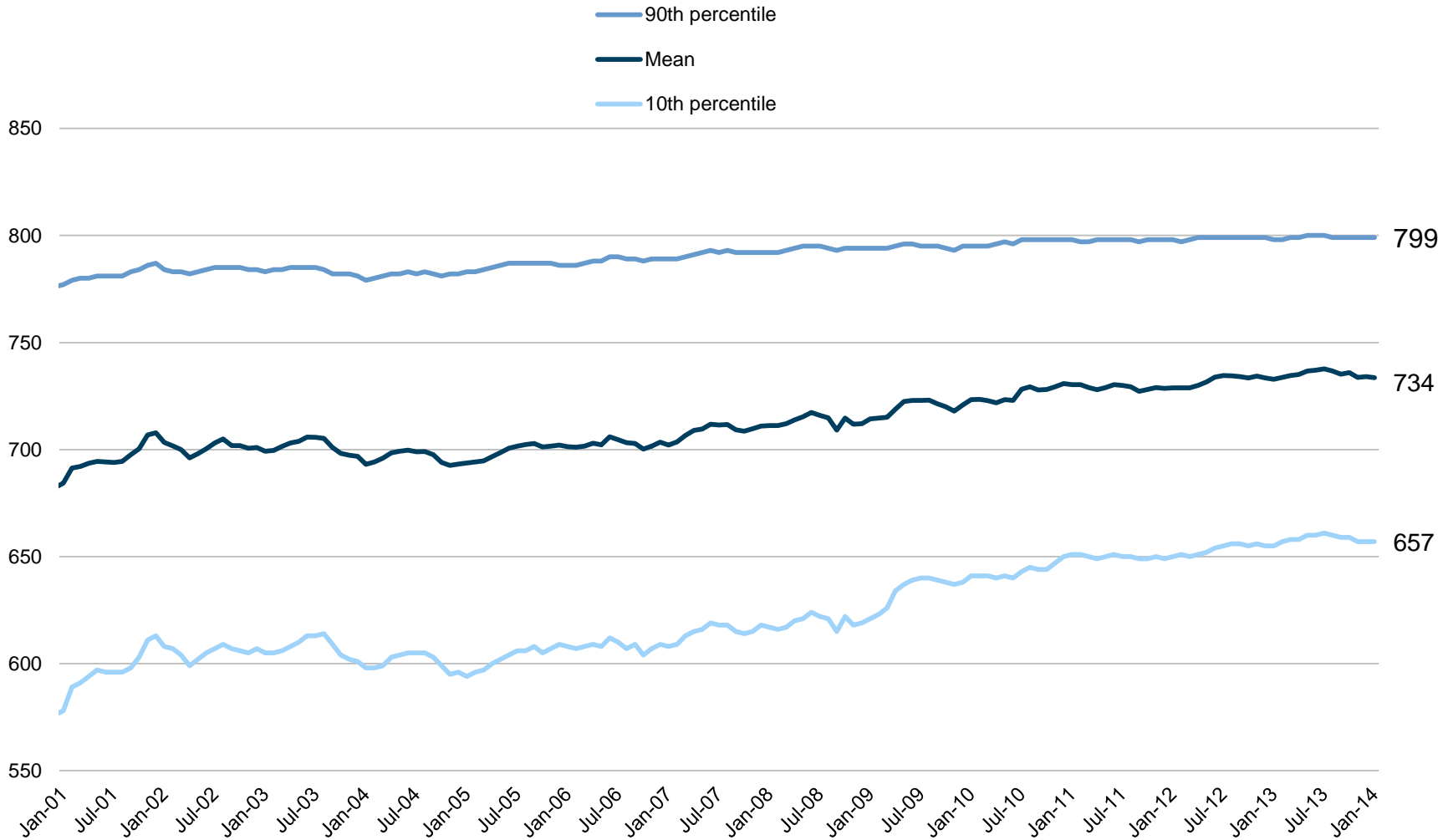
- Total reference pool sizes for STACR deals: \$118 billion in 4 deals
- Total Freddie Mac S.F. outstanding: \$1548 billion
- % partially covered: 7.6%

Class	Amount (\$ millions)	Tranche Thickness (%)	CE (%)	Rating	Initial Spread (bps)
Freddie Mac: Structured Agency Credit Risk (STACR) Debt Notes, Series 2013-DN1 July 24, 2013					
A-H	\$21,906.8	97	3	NR	-
M-1, M-1H, Total	\$250.0, \$54.9, \$304.9	1.26, 0.09, 1.35	1.65	NR	340
M-2, M-2H, Total	\$250.0, \$54.9, \$304.9	1.26, 0.09, 1.35	0.30	NR	715
B-H	\$67.8	0.30	0	NR	-
Reference Pool Size	\$22,584.4	100			
Freddie Mac: STACR Debt Notes, Series 2013-DN2 November 12, 2013					
A-H	\$34,267.5	97	3	NR	-
M-1, M-1H, Total	\$245.0, \$125.9, \$370.9	0.69, 0.36, 1.05	1.95	F: BBB-sf; M: Baa1	145
M-2, M-2H, Total	\$385.0, \$197.9, \$582.9	1.09, 0.56, 1.65	0.30	NR	425
B-H	\$106.0	0.30	0	NR	-
Reference Pool Size	\$35,327.3	100			
Freddie Mac: STACR Debt Notes, Series 2014-DN1 February 6, 2014					
A-H	\$30,980.8	95.5	4.50	NR	-
M-1, M-1H, Total	\$155.6, \$84.4, \$240.0	0.65, 0.35, 1.00	3.50	M: A1(sf); K: A(sf) NR -	100
M-2, M-2H, Total	\$233.4, \$126.6, \$360.0	0.97, 0.53, 1.50	2	M: Baa1(sf); K: BBB(sf) NR -	220
M-3, M-3H, Total	\$264.5, \$143.5, \$408.0	1.10, 0.60, 1.70	0.30	NR NR -	450
B-H	\$87.9	0.30	0	NR	-
Reference Pool Size	\$32,076.8	100			
Freddie Mac: STACR Debt Notes, Series 2014-DN2 April 2, 2014					
A-H	\$26,880.4	95.5	4.5	NR	-
M-1, M-1H, Total	\$230.0, \$51.5, \$281.5	0.82, 0.18, 1.00	3.5	F: Asf; K: A(sf)	85
M-2, M-2H, Total	\$345.0, \$77.2, \$422.2	1.23, 0.27, 1.50	2	F: BBB (sf); K: BBB (sf)	165
M-3, M-3H, Total	\$391.0, \$87.5, \$478.5	1.39, 0.31, 1.70	0.30	NR	360
B-H	\$84.4	0.30	0	NR	-
Reference Pool Size	\$28,146.98	100			

Sources: Freddie Mac and Urban Institute.

Note: Classes A-H, M-1H, M-2H, and B-H are reference tranches only. These classes are not issued or sold. The risk is retained by Fannie Mae and Freddie Mac. "CE" = credit enhancement. Under "Ratings," "F" = Fitch, "M" = Moody's, and "K" = "Kroll Bond Ratings."

Credit Availability: Borrower FICO Score at Origination Month



Sources: CoreLogic Prime Servicing and Urban Institute.
 Note: Purchase-only loans.