

igniting ideas for the mortgage industry.

matchbox

## Matchbox OP(erations) ED(itorial) Page Thoughts and Observations On The Market

2ndary Stress

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What We Do

Fulfillment &  
Advisory Services:  
Mortgage  
Advertising  
Technology  
Consulting  
Hedging

Well, we all knew it was not going to last, but was anyone really expecting this horror show? The sell-off has been fast and furious and nobody is expecting to see 3's again anytime soon. Sure this has happened before, but all of those times have been temporary with the economy still in question. This time the sell-off feels like it has some legs. It looks like we have set new levels without a return to glory. So how is everyone responding to a sell-off of a few hundred basis points within a few days? This week we focus on some action items that (secondary) management should have a handle on.

We strive to keep you all well-informed, as we share our views. Staying a step ahead and running a tight operation are the keys to success in the mortgage banking world, and we are here to help bankers do so. We hope you find our newsletter useful, and if there is anything you want us to cover, [please let us know](#).

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Secondary Stress

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**The Long-Term Forecast-** Now that you have a real live snapshot of your shock report, extend it even further to see what your company will look like if rates shoot up another 50 bps. We're not just talking about pull through shocks for those who hedge, but even simple origination shocks. Lenders spend \$10K-\$100K on insurance policies, but rarely delve into their own business model to see what exposure lies in a volatile market. Forget the locked pipeline for a moment, is anyone forecasting 60-90+ days out?

**Out of Coupons?** Does secondary have a close eye on the locked pipeline and the coupons / rates it has committed? We're pretty confident that there are plenty of 30 year fixed products out there slotted for 3 coupons, now trading with a 96 handle; yikes! Coupons can become illiquid quickly and keeping open hedges can be risky business. Managing the pipeline on a very granular

basis and paying strict attention to how price volatility will impact delivery strategies (BE, forwards, AOTs etc) is key.

**Cost Management-** Think any LOs will allow locks to expire at this point? Will they really press for free extensions, exceptions, or concessions? Will secondary or management give in? For the first time in a long time, secondary is in a position of power; the question is are they strong enough to wield it? Additionally, extension costs can add up quickly if lenders are hedging. Mass extensions on questionable files can quickly become expensive. Time to brush off / tighten up those lock desk policies.

**Proactive Pricing-** So which group do you fall into? Do you freeze pricing? Add internal price adjustments? Or allow the PPE to do all the work? There's one wrong answer here, and if you're unsure which it is - give us a call.

In these volatile times it's critical to keep track of the market. Meeting to discuss how to handle the business in this market is important, but missing a rally or a sell-off after being tied up in management meetings can be extremely costly. Secondary managers need a true pulse on the market. Oh, that means having access to live market pricing indications too - something a bit more sophisticated than the text messages that most LOs are receiving.

**Proactive Margins-** Some are already cutting margins in effort to keep the wheels of the pipeline greased. Others are adding margin until the market stabilizes a bit. And there are a few who are micro-managing margins based on investor outlets and particular products. While each of these strategies have their own pros/cons, it's only cutting margins that gives us great concern.

**Know Your Data-** Purchase vs refi? Cash out vs rate/term? Expiration dates, status levels, etc - the details have never been more important. Possibly the most important data point of all is rate. Not just for the aforementioned exposure related to illiquid coupons, but also due to compliance. In-touch secondary groups are concerned over HPML loans and for those in NY, dreaded NY Subprime Home Loan testing. We can guarantee there have been loans locked over the last few days which cannot close as they'll certainly fail compliance testing and be deemed unsaleable.

**The Future Of Originations-** Call centers? Internet leads? Radio or Print Campaigns? What does the future hold for these strategies? We're not sure of the economics here, but we do know that lenders best be careful not to throw good money after bad; doubling-down on a high risk origination strategy in a volatile market. Does it make sense to increase the advertising spend to just keep the pipeline moving?

**Q3 Liquidity-** June ends this week followed by a long July 4th weekend. It will be July 10th before we know it and with the Western Secondary approaching, July will come and go quickly, but not before there are some substantial cash flow anomalies. For those who hedge, and do not deliver AOT, loan sales will be coming in 300-600bps light. Those won't go down easy. On the other side, pairoffs from broker dealers will be substantial. Secondary and accounting better be expecting this ripple effect

on liquidity and cash flow.

It is easy to be a Monday morning quarterback and highlight all of the things that you should have done to avoid this, but the most important thing to do now is attack the pipeline and be proactive with pricing, policies, forecasts and even EDUCATION. Sales will need explanations. They need to speak intelligently to their clients and understand how best to manage their pipelines in the future. Be proactive and communicate.

### About Us:

Matchbox is a collection of gritty industry veterans who decided to create a company aimed at helping mortgage companies ignite ideas that are outside the box to realize their true potential. We have years of real life, hands on experience in the business, and we want to offer our keen insight to others as they take on the challenges before them.

As individuals, we each contribute unique perspective and expertise. Collectively we provide a true roadmap to success, regardless of your current situation. Like any master craftsman, we are very passionate about our work and we approach each client as if your company were our own. In the end, we help you, be a better you.

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