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Thoughts and Observations On The Market

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December 18, 2013

Oh boy, heading into Christmas with our last newsletter of the year we wish there were better things to write about. Earlier this week Fannie and Freddie posted their new LLPA grids effective early 2014. Some Secondary Managers are already scrambling with their analysis which isn't looking pretty. The ramifications and unintended consequences can have some far reaching effects. And if the agencies are also bumping the g-fee (a bit of clarity out be nice) we're looking at a pretty nasty right-left hook combination from FHFA and the GSE's. As always, we believe in forecasting and being prepared.

We know that you receive a lot of information on a daily basis and we appreciate that you continue to read what we have to say. We wish you and your families a happy and healthy holiday season.

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.

On The Rise - LLPAs & G-Fees

Well here it is, but we warn you - it's not pretty. A few weeks ago we were concerned with the announcement of a 10-14bp increase in the g-fee which would lead to a price hit of approximately 40-70bps or an increase of .125-.25 in rate. The announcement was somewhat tempered by the removal of adverse market fee / LLPA for most states. The net impact would have no doubt pushed interest rates higher. Taking a closer look at the updated matrix, there are some obvious revelations.

Have the GSEs learned the secondary "smoke and mirror" pricing strategy? Yes, the adverse market fee is removed (outside of CT, FL, NJ, & NY) but every term >15 years has an increased LLPA adjustment of a minimum of 25bps. In the day to day trenches, removing the adverse market fee is pure window dressing. And for those in the northeast and the snow-birds in FL, this is a compounded hit.

We are accustomed to the LLPAs addressing risk-based pricing with low fico/high ltv tranches, but this udpate is different. In a world of pristine credit quality, we're seeing some of the higher credit tiers impacted the most. The 680-740+ tiers will feel this updates much more than the 620-679 tiers. We noticed with any loan over 70LTV, count on LLPAs up at least 50bps. Apparently, there's no such thing as a vanilla loan these days and a 720+ fico is still a substaintial credit risk. A 740 fico at 85LTV will have a 150bp LLPA, up from 25bps. OUCH!

The net effect here is a move to increase conventional rates, much more than initially expected. Our take? It is by far the most significant step FHFA and the agencies have taken to date in their efforts to better align the conventional market with the private sector. Many of these LLPA updates will push rates .25-.375 higher (i.e. worsening price 75-150bps). This is before accounting for any actual g-fee updates which we'd expect to have another .125 or so impact on rates.

As lenders look to forecast their goals and expectations in 2014, this is no doubt a curveball that poses some new questions. Some critical thoughts for not just Secondary Managers, but Owners and Sales Managers:

-How will these LLPA's be phased into pricing models and PPEs? Allowing time to take its course is a terrible strategy.

-How can lenders best arbitrage the LLPA variance and maximize delivery / pricing under the current LLPAs?

-Will this impact my hedge / mandatory execution? It's certainly possible considering the above items. It will also lead to the need of refreshed pricing policies (extensions, re-locks, worst case, etc) as exceptions can be extremely costly and impact hedge reporting.

-How will a .375-.5 increase in rates impact the business? Volume projects, marketing campaigns, sales strategies, education, staffing, etc will need additional attention.

-Will these updates impact QM/ATR? Of course they will but how will these be monitored, tested, or more importantly, documented? With some of these LLPA updates, obtaining par rates and bona fide discount points may be difficult. LLPAs of 150-300bps will be all too common.

-Will certain opportunities fizzle out? Will new opportunities arise? Yes and Yes!

-Is there any silver lining here? Of course, we would imagine that MSR portfolios would see an uptick in valuations.

Q3 and Q4 were tough for many lenders, lower volume stressing sales and volatility/higher rates stressing secondary departments and execution performance. With new regulations and updates, err increases on the LLPAs and g-fee, creating a realistic forecast and strategy as we enter a new year has never been more critical. It's a seasonally slow time in the market so we hope management can dedicate some time to this as we know that those who prepare will prosper while others will struggle.

We're here to lend a hand, provide an independent sounding board, and offer perspective to those looking for some guidance or confirmation of direction.

Relying On Reports? Better Know Your LOS

Last week Rob Chrisman's newsletter and MIAC shed light on a concerning topic - reporting on lock cancellations and their reported impact on pull through. On a more macro level, the concern really speaks to data integrity and the reliability of reporting. As any lender will attest, especially Secondary Managers, their world revolves around reporting and data integrity. LOS systems have thousands of inter-connected fields and often reports are developed by an admin, who doesn't REALLY appreciate the importance or reasoning for the data being requested.

Data points are not simply defined and may be captured in different places. Encompass has at least two fields for lock date, and arguably more between buy side requests & confirms and sell side execution. While these multiple fields may seem confusing, they are important for anyone looking to to have strong reports and therefore need to be well understood. The same goes for lock days, cancellation dates, old vs new expiration, renegotiation dates, and re-lock dates. How about closing dates, note dates, funding dates, document dates etc?

Some Secondary Managers will take it upon themselves to create their own reports without understanding all of the field options and functionality. Either way, whether it's the admin or a Secondary Manager (or any user for that matter) that is creating the reports, many lenders are left with data that can cause exposure due to data fields, user process flow within the LOS and reporting rules/filters. The root of the problem is that the exposure is unknown and difficult to find. Even after this note was included in Chrisman's daily newsletter, about a dozen lenders reached out to ask if they were using the right or wrong fields for their reports.

Truth be told, we're not sure which is more concerning, possibly managing a pipeline with inaccurate reporting or not having the oversight or audit functions to highlight these data deficiencies. LOS updates are constant, with new integrations and new fields/functionality. Rarely do we see lenders/secondary groups running a reliable audit on their pipelines. It is very scary to think that lenders may not have a close handle on their own locked pipelines, but if the reports are flawed to begin with, it's really tough to know your pipeline and perform an audit. It is not uncommon for us to work with lenders that have 10-30% of their pipeline exposed simply due to inaccurate reporting. In a volatile market that has pressure to push rates higher, this is quite scary.

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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