



The Perfect Storm
 Northern California Chapter of the Appraisal Institute
 October 28, 2008
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The Mortgage Industry
What Happened?
What has the Fed done?
Where are we going?
How do we get there?

The Perfect Storm
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Wholesale Mortgage Banking and Brokering

- Represent Banking, Wholesale, Credit Unions, Thrifts and Private Money....
- Correspondent Channels...Banking
- Used to be that All Retail Banks had a Wholesale Channel.....No More!!!
- US Bank, Wells, Countrywide, Chase,
- Recent exits...Citi, Downey...Liquidity!!!

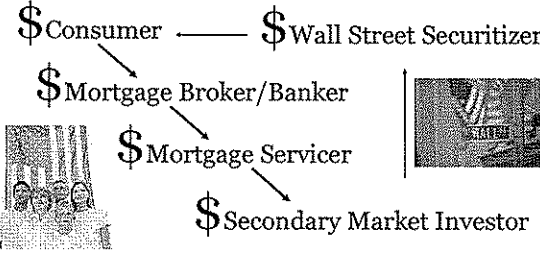


Types of Mortgage Products

- Fannie/ Freddie You Own!!! Through Retail Banks, Wholesale, Credit Unions
- Portfolio Products 40 year, 5/5s etc
- ALT A....No More!!!!
- Sub Prime B Paper....No More!!!!
- Stated Income....Virtually Gone!!!
- Private Money Sourcing

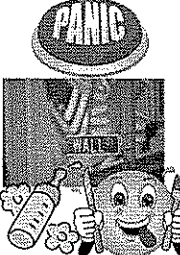


Understanding the US Mortgage Market

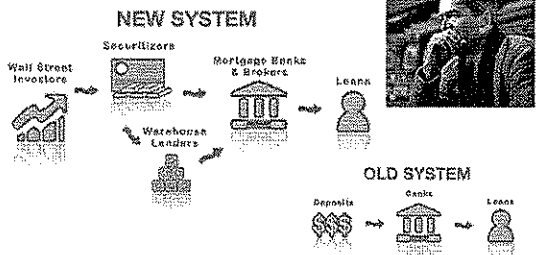


Credit Crunch: What Happened and Why?

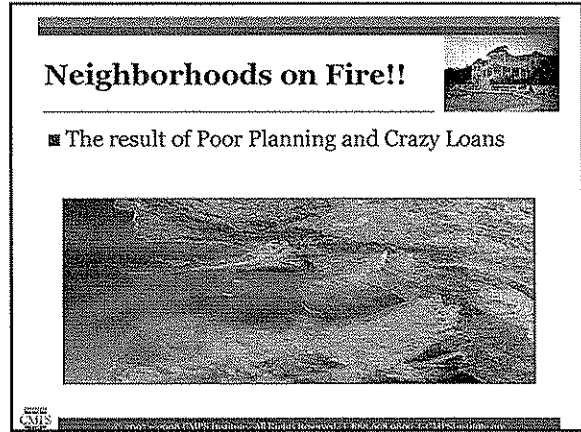
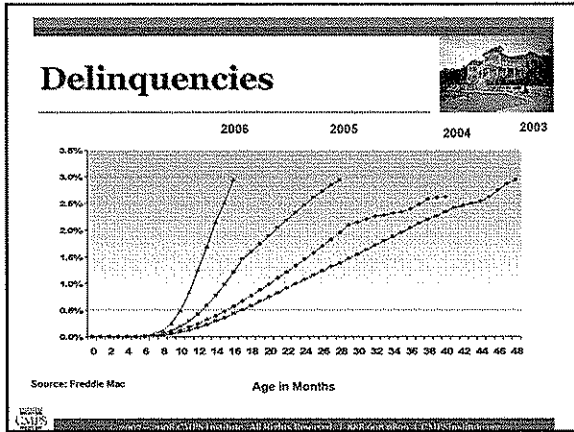
- Wall Street Got Very Hungry
- Mortgage Banks Fed the Appetite
 - Reckless Lending Guidelines:
 - No Credit, No Income, NO PROBLEM!!
 - Consumers Got in Over Their Heads
 - House Prices go up, so JUST REFINANCE!
 - Housing Market Slowed Down
 - Oops! Can't Refinance... FORECLOSURE TIME!!
 - No Incentive to Protect Equity That Has Evaporated!!
- Wall Street Got Sick and Caused a Run on the Mortgage Banks



Where is George Bailey When You Really Need Him Most??



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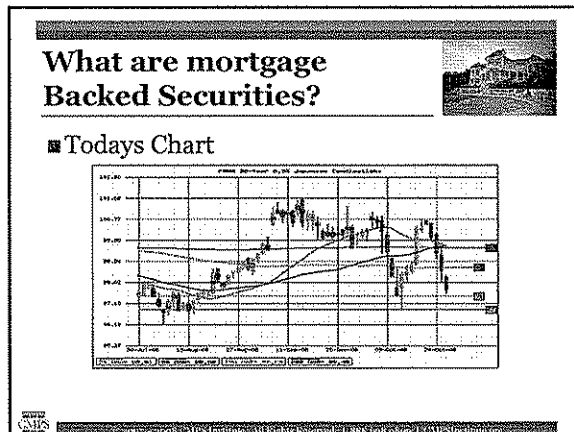


Making the Complex Simple: CDO, CDS, SIV, MBS!!!!

- Think Baseball Strike
 - Broadcast TV
 - Broadcast Radio
 - Hotdog Stands
 - Jerseys & Baseball Caps
 - Baseball Cards Etc

The Technical Why... Types of Mortgage Investment Vehicles

- MBS Mortgage Backed Securities. Bundled Mortgages
- CDO's Collateralized Debt Obligations... Sub MBS
- CDS's Credit Default Swaps (Insurance Policies, Hedges)
- SIV's Structured Investment Vehicles. Separate Ventures LLC's
- The Money Machine



CDO: Collateralized Debt Obligation (CMO, CLO, etc.)

- Pool together different types of bonds
 - Receive income
- Divide the default risk into different "tranches"
 - Divide up the income into multiple packages
- Sell the "tranches" to investors
 - Sell the packages and make a profit

CDO: Collateralized Debt Obligation

- Approx. 80% of securities in CDOs were MBS; around 70% of which were Alt-A, subprime, and 2nd liens
- Senior tranches priced at only 10 - 25 bps (0.10% - 0.25%) above 10 yr Treasury notes!
- Crazy Investors!! Confidence in Real Estate

The diagram shows a \$100mm MBS being split into three tranches of a \$100mm CDO:

- \$80mm tranche:** Safe until you hit 20% defaults. Lowest Yield, AAA rated.
- \$15mm tranche:** Next 15% of defaults. Intermediate Yields.
- \$5mm tranche:** First 5% of Defaults. Highest Yield.

SIV: Structured Investment Vehicle

The diagram shows a central circle labeled "SIV" with two arrows pointing to it from ovals: "Borrow money by issuing short-term debt" and "Invest money by purchasing long-term debt".

- What happens when the Long Term Debt Goes Bad!!!!

Perspective

- \$45 trillion CDS market!
- \$750 trillion World Wide derivatives market!
- 30 to 1 leverage among investment banks is not uncommon
- Investment banks move activities "off-balance sheet" with SIV's, CDO's, CDS's and other derivatives..It's a hidden Business Model....
- Hedge funds - \$2 trillion equity
 - 60% of all trades in the CDS market and 1/3 of CDO trading
 - Investment banks make 20% - 30% of their revenues from hedge funds

Fed Bailout?

- Bear Stearns biggest counterparty in the CDS market
- If they fail, what next??!!
 - Moral Hazard vs. Economic Catastrophe... Restore Confidence, Prevent Disaster
- The Fed helps consumers by helping Wall Street??!! Helped chase buyout Bear Stearns

George Bailey a/k/a Ben Bernanke to the Rescue!!


The flowchart titled "NEW SYSTEM" shows the flow of capital: "Wall Street Investors" provide funds to "Securitizers", who then work with "Warehouse Lenders" and "Mortgage Banks & Brokers" to originate "Loans".

The Role of the Fed



The diagram shows "The FED" at the center with arrows pointing to various activities: "Regulating Bank Reserve Requirements", "Lending Money (Checks) to Banks through the 'Discount Window'", "Open Market Activities", and "The Term Auction Facility".

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The Fed Takes Historic Measures




- Discount Window "stigma" Poor Banks, Hurt Animal
- Term Auction Facility No Exposure Highest bidder
- Term Securities Lending Facility
 - Non-depositories
 - Non-agency MBS allowed as collateral Not Liquid at this time

OK - So What is the Impact of All This?



- Flight to Quality in the Investment Markets
 - Lower rates on traditional conforming loans
- Much Greater Emphasis on Credit Score
- Many Sub-prime, Jumbo and Alt-A Loan Programs Have Evaporated
 - Higher rates and costs for higher-end home owners, investors, self-employed borrowers, etc.
- HELOCs are Being Arbitrarily Closed by Lenders
- Extra Pressure on Home Prices Due to Foreclosures, Restrictive Lending Guidelines, & Glut of Speculators
 - Great Depression = 25% Unemployment Rate!
- Increased Government Regulation




Pending Legislation




- FHA Reform -
 - S 2338, HR 1852, and HR 1427
 - GSE Reform (Gov't Sponsored Enterprises)
 - Higher loan limits on FHA loans
 - Reverse Mortgages
- Mortgage Industry Reform
 - HR 3915 Brokers Yield Spread
 - Various State Legislatures
 - Appraisal Guidelines and Policy




Higher Loan Limits





- HR 5140 - Economic Stimulus Package
 - Increase FHA and Conforming Loan Limits in High Cost Areas to as High as \$729,750 Jan 1 going to 625K
- Problems:
 - Pricing
 - Guidelines
 - Expires December 2008
- Solutions:
 - May 2008 Fannie Mae Guideline Updates
 - Consider LIBOR ARMs for Jumbo clients




Elimination of Tax on Forgiven Mortgage Debt





- HR 3648 - Mortgage Relief Debt Forgiveness Act
 - \$250k Home Value
 - \$300k Mortgage Balance
 - \$50k Difference
- Guidelines:
 - \$2mm on Principal Residence Acquisition Indebtedness
 - Expires January 1, 2010


Options for Troubled Clients




- Foreclosure
 - Late payments
- Deed-in-Lieu
 - Maybe late payments
- Short Sale
 - Sell on open market
- Loan Modifications
 - Renegotiate terms with mortgage lender


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Product Options, the Bright Side..... 


- More Products than one might realize
- Great rates in the mid 5% to Low 6% Range
- 15,20,30,40 year products
- Interest Only!!!
- Jumbo Loans to 4 Million
- Stated Conforming and Jumbo at 80%!!!
- 97% LTV FHA Programs (Gift Allowed), 96.5% Jan 1
- 100% Rural Loan Programs
- Private Money

Credit Issues 


- What Credit Issues?
- FHA down to 580 Score!!!
- BK at 2 years!!
- 60% LTV or Less Fewer to no Hits on Pricing
- Awards for 720 Ficos

Lender Sources 


- Over 285 Wholesale Lenders down!!!
- Still Plenty of them to go around...???!!!
- Daily Parameter changes....Makes things tough
- Vanilla Loans, Still hard...
- Lenders that look for Problems

Rates..Where are they going? 



- Up or Down?
- All Types of Rates...
- Do Rates go Down when Fed Lowers?
- Why Rates Change...the Real Reason

Home Valuation Code of Conduct 

- Who Started this?
- Is it a Government Mandate?
- Is it in a reform package?
- January 1, 2009
- Broker Relationships
- Will it be Implemented?
- How will it Effect the Mortgage Industry?
- Who Benefits?

Humans = Emotion 

- Greed
 - Wall Street
 - Mortgage Industry
 - Consumers
 - Government
- Fear
 - Wall Street
 - Mortgage Industry
 - Consumers
 - Government

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Making it Happen



- Only 15% of Wholesale originators remain!!
- The Road to Growth is filled with Client and Lender snags!!!
- Navigating, Planning, Networking and Budgeting
- Keeping Positive....Make it Happen!!!

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