The State of the Market with Amie McCarthy

March brought the vernal equinox and unprecedented interest rates and market volatility. The housing and mortgage market seemed to be heading for a historic year. The week of February 6, the 30-year fixed rate reached its lowest since 2012 at 3.45%. The last week of March, rates were 3.5%. Rates dropped to 3.33% in the first week of April and dropped again to 3.31% as of April 16. New purchase activity slumped 10%, as the employment market contracted and demonstrated the damage the coronavirus is having on the US Economy. Mortgage applications increased 15.3%, week over week, but the purchase market index fell 24%. Lien release volumes are up and will continue to do so with the favorable rate environment. The United States and the world are employing tactics to reduce transmission of the COVID-19 virus, which is directly impacting employment, and the markets. Even once things are more under control, furloughs and loss of income will reduce consumer's ability to obtain government-backed loans, and the non-qualified or unconventional market may not be able to serve these borrowers due to market liquidity issues. The spring purchase market is going to be tough, but the refinance market will hopefully sustain the impact. However, estimates from FHFA have projected delinquencies higher than the credit crisis, which started in 2007.

In an attempt to stabilize the markets and keep borrowing costs reasonable due to our current health crisis, Federal Reserve Chairman Jerome Powell employed tactics that were not leveraged since the 2008 financial crisis. Powell effectively cut the benchmark by a full percentage point to zero. The Fed is also employing QE or quantitative easing, a tactic in which the United States central bank purchases billions of dollars in bonds to keep funds flowing and rates low. The Fed will be purchasing up to $40 billion in agency MBS (Ginnie Mae, Freddie Mac, and Fannie Mae), which makes up about two-thirds of the market. Yields have returned to normal after a wild ride for the last few weeks. The NY Fed also purchased $1.04 billion in CMBS to support the commercial real estate market, which will be deeply affected by hotel, mall and other commercial property vacancies and potential delinquencies. For our industry, low-interest rates are fantastic. However, the secondary market is deeply affected.

Transaction services to support whole loan and mortgage servicing rights (MSR) sales and transfers have slowed. Over the last few months, due to increased prepay speeds, mortgage servicing rights (MSR) values are down, and whole loan trading of re-

performing and non-performing loans has slowed. The 10 year Treasury yield was 0.70% as of March 31, indicative of fast prepay speeds and record low MSR valuations.
Even selling service released is not economically advantageous, with Service Release Premiums (SRP) recently hitting zero. Non-banks and REIT's who are short on cash, are feeling the pressure and experiencing margin calls. Unless broker-dealers relax their requirements, it will lead to a significant market disruption to the unconventional market. The non-qualified (Non-QM or non-conventional) mortgage players are already feeling the squeeze. Non-QM originators are experiencing a pullback from warehouse lenders, and a handful of lenders have put originations on hold.
The United States mortgage finance system needs assistance, which is not addressed in the Coronavirus Aide, Relief, and Economic Security Act (CARES). Lawmakers are allowing homeowners to delay their payments. Still, they have no assistance for the mortgage servicers who must advance the principal and interest due to bondholders from their funds when payments are not received from consumers. The bill provided for $454 billion for the Treasury's emergency lending program for large corporations, however, mortgage lending was not included, even though the industry lobbied for assistance.

The government agencies in mortgage finance reacted to address the health crisis. HUD announced on March 18 that all foreclosures and evictions would be suspended for 60 days in reaction to COVID-19. Government mortgage finance agencies are preparing for potential missed payments from consumers.
Ginnie Mae created The Pass-Through Assistance Program (PTAP) to address the issuer's potential liquidity issues for participants of the Single-Family MBS Program. The PTAP enables issuers to finance advances due to pools, for principal and interest payments not received from borrowers, at favorable terms. This liquidity facility will provide necessary assistance to issuers; however, if the unemployment rate continues to rise, and origination of pooled eligible loans drops, issuers may have difficulty repaying in the future.

Ginnie Mae also allows for a note securitization structure in which the owner of the MSR issues participation certificates, which represent the beneficial interest in some component of its MSR's. This may include interest in the principal and interest and corporate advance receivables. The resulting participation certificates are sold into a trust, pursuant to a repurchase agreement. This is a vehicle for Ginnie Mae issuers to have another source of financing or their MSR's and to offset advances which they are obligated to pay, in the event a borrower does not make their payment.
The FHFA, who oversees Fannie Mae and Freddie Mac, is not making any moves to assist non-bank mortgage servicers, which may lead to additional market consolidation. The GSE's have guided consumers who are impacted by COVID-19, under the direction of the FHFA. Impacted borrowers by COVID-19 have the option to either request forbearance for up to six months, not incur late fees, will not be reported late to the credit bureau reporting agencies, and all foreclosure or legal proceedings will be suspended. There is also the potential for a longer-term modification solution, in the future from the agencies, as well.

The CARES Act provides support to both consumers and businesses. Specifically, consumers with incomes up to $75,000 for individuals and $150,000 for married couples, may receive $1,200 for single taxpayers, and up for $2,400 for couples, plus $500 per child. Extended unemployment will be offered in the amount of $250B, and expands eligibility, and offers an additional $600 a week for four months, and extends benefits until December 21, 2020. It also applies to self-employed, independent contractors, and gig economy workers. The bill waives the 10% early penalty withdrawal up to $100,000.00 for coronavirus related purposes, retroactive to January 1, but does not wave taxes. Taxes will be spread over three years.

Also, 401K loans for coronavirus are increased from $50,000 to $100,000. Required minimum distributions from IRA's and 401K's at age 72, are also suspended. Charitable contributions limits are changed, and there is a provision that provides an above the line deduction. From a healthcare perspective, all testing and potential vaccines for COVID-19 will be covered at no cost to patients.

For businesses, employers can delay payroll taxes on a portion of their 2020 payroll until 2021 and 2022. Small businesses have $350 billion dedicated to preventing layoffs and closure while employees remain at home per state mandates. Companies with 500 employees or fewer than maintain their payroll will receive up to 8 weeks of cash flow assistance. The Tax Cuts and Jobs Act (TCJA) net operating loss or rules are modified. The 80% rule is lifted, and losses can be carried back five years. The Excess Loss Limitations (ELL) rules for pass-through entities are suspended. The interest expense limitations are increased to 50% from 30% for tax years 2019 and 2020. For large corporations, $500 billion is allocated to provide loans, loan guarantees, and other investments. The Treasury Department inspector general will oversee the program. The loans will not exceed five years, and will not be forgiven. Ten percent of $50 billion is earmarked for passenger air carriers and $8 billion for cargo carriers.

American hospitals and the US healthcare system will is allocated $140 billion, which will initially be injected into hospitals. The remainder will be providing personal and protective equipment for health care workers, testing supplies, investments in human capital, training, accelerated Medicare payments and supporting the Center for Disease Control. (CDC). Local, state, and tribal governments will receive $150 billion. States and educational institutions will receive $30 billion. Disaster relief funds of $45 billion and $25 billion for transit programs. The Agriculture Department can increase its bailout program from $30 billion to $50 billion.

Our industry is resilient and is pivoting to manage the heightened volumes of refinancing applications, and requests for assistance. Some realtor associations are advising clients to extend home purchase contracts to allow for delays. The GSE's have eased appraisal guidelines to enable the transactions to continue to flow without a traditional appraisal. Firms with online lending platforms are continuing to deliver for customers. Business process outsourcing firms, which enable online notarization and remote closings, are seeing an increase in adaption. More than twenty states allow for electronic notarization. In March, a federal bill on electronic notarization was introduced in the Senate. Origination and servicing firms are seeing unprecedented volumes and are leveraging business process outsourcing firms and technology more than ever. Fortunately, having partners to provide critical transaction documentation, such as assignments and lien releases, and portfolio transfer support enables banks and servicers to focus on their customers and bottom line.

The mortgage industry is entering a time where government-backed loans may overtake the non-conventional market again, and underwriting criteria will likely tighten. The Fed is ready to keep credit flowing by assuring lenders there is a buyer for mortgages being closed. The next few months will be challenging for mortgage origination and servicing, attempting to handle applications and managing the financial impact of borrowers missed payments due to the health crisis at hand. As of the publication date of this article, rates are at a historic low of 3.31%. The mortgage rate environment will continue with historic lows, allowing for borrowers who have equity to cash out and get a lower rate for those who qualify. Unfortunately, due to the health crisis we face, the spring and summer purchase market may not be as robust as predicted.

About the Author:

Amie McCarthy is the Vice President of Business Development - Capital Markets at Nationwide Title Clearing, Inc. and has more than two decades of experience in mortgage finance, structured products and banking. Her core competencies include primary and secondary marketing, underwriting, valuation, servicing, securitization, and regulatory compliance. She brings product life cycle experience, which NTC's clients leverage to improve processes, controls, overhead and best execution on mortgage transactions. She has worked from Wall Street to Washington, for investment banks, a GSE and regulator.

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