

SFA Research Corner

A Tale of Two Mortgage Markets

April 7, 2021



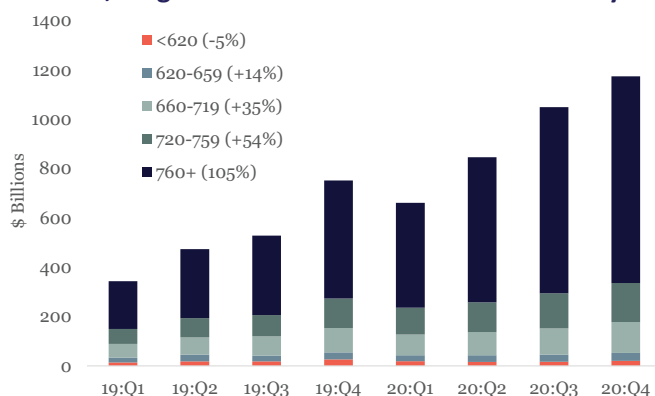
WHAT WE'RE WATCHING

On April 2, the *Wall Street Journal* [reported](#) that while “[t]he mortgage market is humming ... getting approved for a home loan is as difficult as it has been in years.” Moreover, “[b]orrowers with credit qualifications that fall just outside the stellar category are finding fewer lenders willing to approve their applications.”

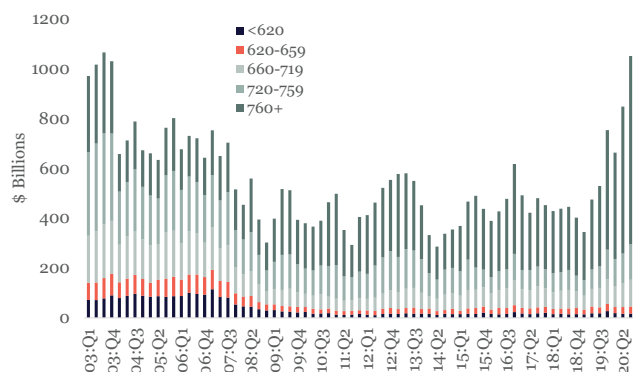
The Federal Reserve Bank of New York reported similar findings in its February 2021 [Quarterly Report on Household Debt and Credit](#), using data from Equifax. Between 2019 and 2020, mortgage originations for prime borrowers saw the strongest gains – origination levels for borrowers with the strongest credit profile (credit scores of 760+) doubled as volume for the second strongest credit tier (720-759) saw a 54 percent gain. Over the same period, the origination levels for borrowers with weak credit profiles either dropped or saw only modest growth – the number of borrowers with the weakest credit scores (less than 620) fell by 5 percent as originations for borrowers in the second weakest credit tier (620-659) grew by 14 percent. The number of borrowers in the middle credit tier (660-719) increased by 35 percent.

2019 Versus 2020

YOY Mortgage Originations for Highest Credit Tier Doubled, Originations for Lowest Credit Tier Fell by 5%

Source: [New York Fed Consumer Credit Panel/Equifax](#)

4Q 2020 Origination Volume Surpassed 2003 High; Composition of Loans Very Different

Source: [New York Fed Consumer Credit Panel/Equifax](#)

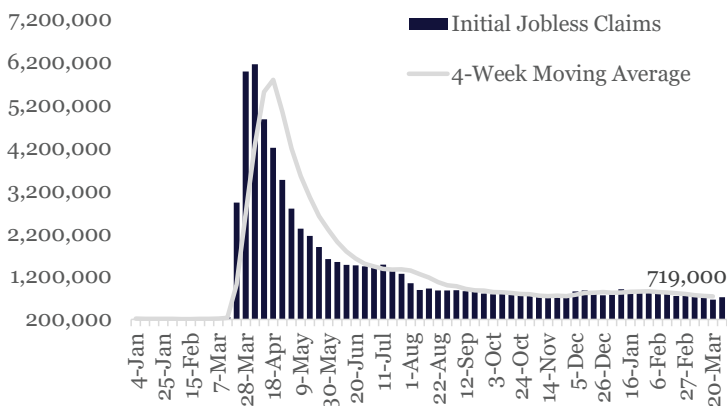
From a historical perspective, the origination volume in the fourth quarter of 2020 easily surpassed the previous high recorded in the third quarter of 2003. However, as [economists at the NY Fed](#) note, “although these two bumps in mortgage originations are similar in magnitude, the composition is quite different; 71 percent of originations in the fourth quarter of 2020 went to borrowers with credit scores over 760, while in the third quarter of 2003, only 31 percent of those new mortgages went to the most creditworthy borrowers.”

Since the financial crisis, borrowers with lower credit scores have been faced with a tight credit environment, a point addressed by the [Consumer Financial Protection Bureau](#) in crafting its Ability-To-Pay Rule. The Bureau noted then that “tight credit remains an important factor in the contraction in mortgage lending over the past few years.”

The COVID-19 pandemic has only exacerbated this trend. Historically, natural mortgage delinquency rates have closely tracked the unemployment rate. Faced with high levels of pandemic-related joblessness, lenders have been forced to shy away from taking on more credit risk even as green shoots of recovery continue to appear in the economy. [The Senior Loan Officer Opinion Survey on Bank Lending Practices](#) reported in January 2021 (the most recent survey month) that the net percentage of banks tightening lending standards for subprime mortgages was 14.3 percent. Compare this with 1.8 percent for prime non-QM, non-Jumbo loans.

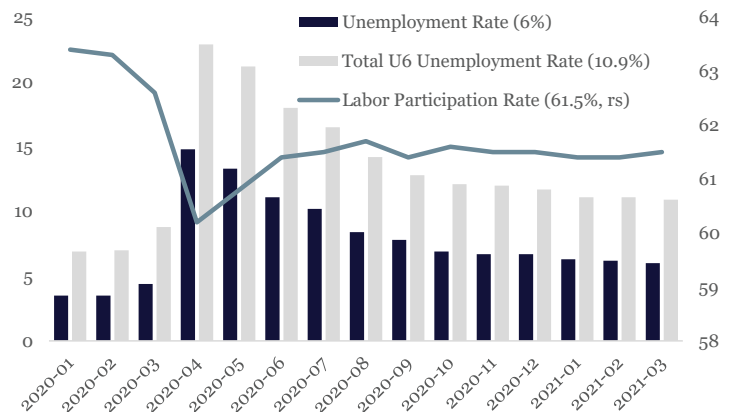
As the labor market recovery stagnates and jobless data remains stubbornly high, we expect tight lending conditions to continue for subprime borrowers. For the week ending April 1, initial jobless claims [rose](#) 61,000 to 719,000. Despite the marked improvement from the 6.1 million jobless number recorded in April 2020, today’s number stands three times above the average recorded in the pre-pandemic months of January and February 2020. The unemployment rate has shown a similar pattern. Although the March headline rate inched lower to 6 percent, the number of permanent job losers is little changed month over month at 3.4 million as the labor force participation rate remains depressed at 61.5 percent. While [job growth](#) was widespread in March, bringing employment across most sectors within 5 percent of levels recorded in February 2020, employment in leisure and hospitality remains down 3 million, or 19 percent. Total non-farm employment is down 8.4 million from its February 2020 level.

Initial Jobless Claims Stubbornly High March 27: Rise 61K to 719K



Source: [Department of Labor](#)

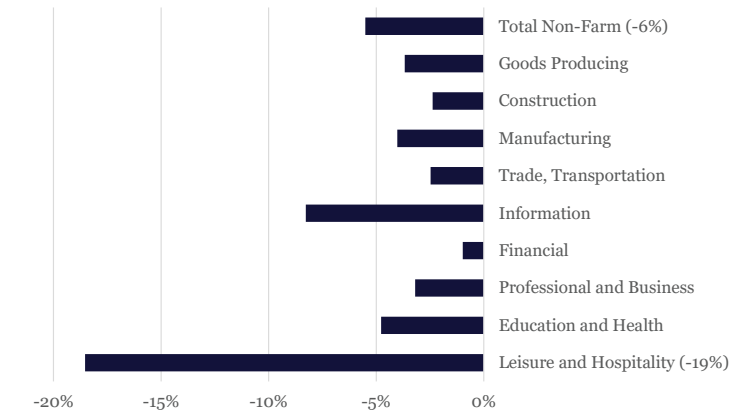
Unemployment Rate Improves Incrementally; Labor Participation Rate Little Changed



The labor force participation rate is the percentage of the population that is either working or actively seeking work. The total (U6) unemployment rate includes total unemployed, plus all persons marginally attached to the labor force, plus total employed part-time for economic reasons, as a percent of the civilian labor force plus all persons marginally attached to the labor force.

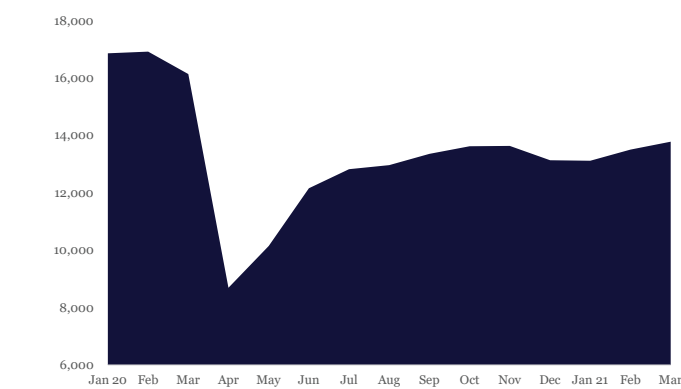
Source: [Bureau of Labor Statistics](#)

Change in Employment by Industry:
Today Versus February 2020



Source: [Bureau of Labor Statistics](#)

Leisure and Hospitality Sector Adds 280K Jobs in
March, Down 3.1MM Jobs Versus February 2020

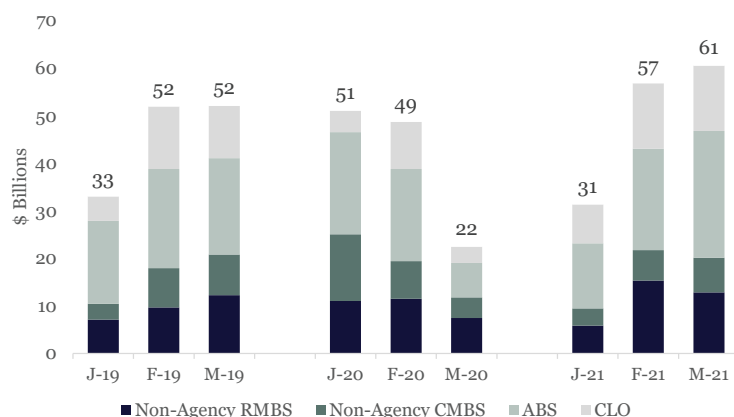


Source: [Bureau of Labor Statistics](#)

MARKET SUMMARY

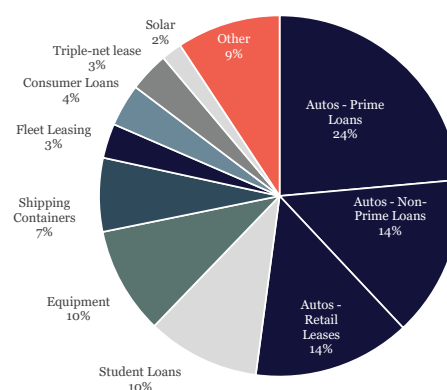
A flurry of issuance in the last week of March brought new-issue volume to \$61 billion for the month. At the end of the first quarter, issuance across non-agency RMBS and CMBS, ABS, and CLOs stand at \$149 billion, easily exceeding 1Q 2020's volume of \$122 billion and 1Q 2019's volume of \$137 billion. SOFR issuance has reached \$28 billion, led by Freddie K CMBS bonds. Bond pricing and bid-ask spreads in the secondary non-agency markets remain range-bound.

Issuance for Non-Agency RMBS and CMBS, ABS, and CLO 2021 YTD (\$149 Billion) Versus 2019, 2020



Source: Market Compilation

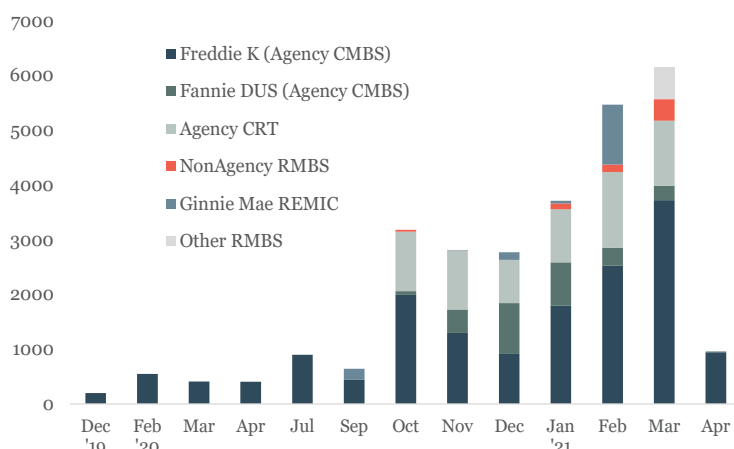
ABS Only 2020 YTD: \$56.5 billion



Other includes ABS backed by aircraft lease, insurance premium, rail lease, tax liens, UK/US credit cards, and litigation funding, whole businesses, timeshare, venture debt, PACE financings, data center financings, and insurance premiums.

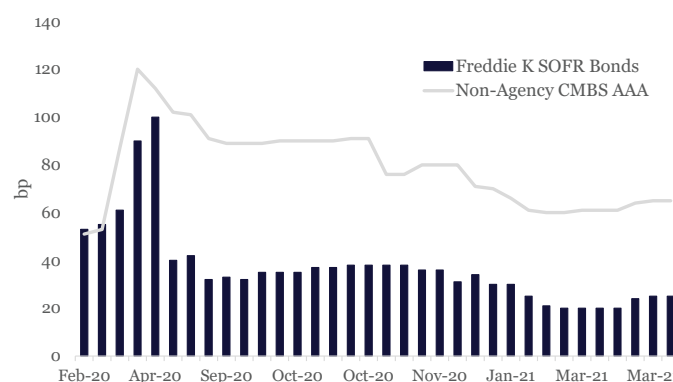
Source: Market Compilation

SOFR-Based Securitization Volume 2019 to Today: \$28 Billion

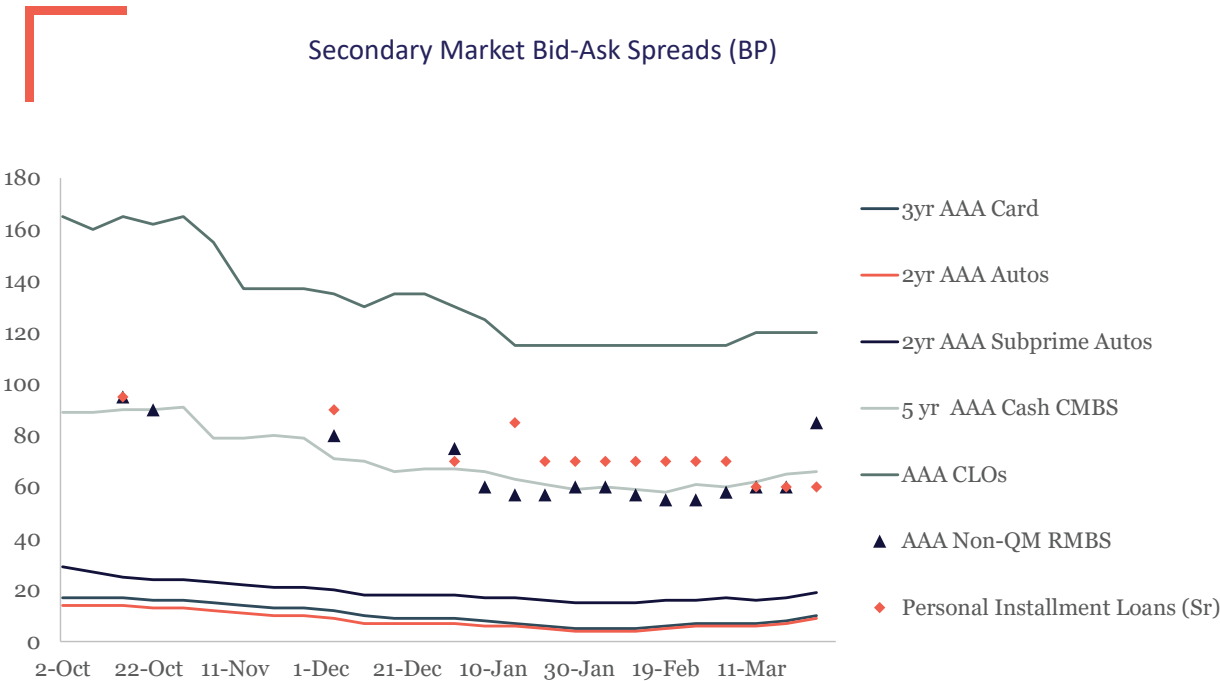


Source: Market Compilation

SOFR Pricing (BP) Freddie K Versus Non-Agency CMBS Triple-A



Source: Market Compilation



Secondary Market Bid-Ask Spreads		
(bps)	26-Mar	19-Mar
3yr AAA Card	10	8
2yr AAA Prime Autos	9	7
2yr AAA Subprime Autos	19	17
5yr AAA Cash CMBS	66	65
AAA CLOs	120	120