STRUCTURED FINANCE ASSOCIATION

SFA Research Corner

Housing Market Seesaw and Securitizations—Sales Down, Equity Up

November 9, 2023

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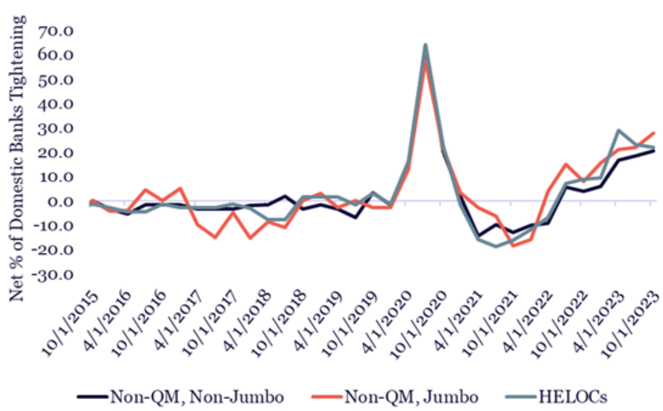
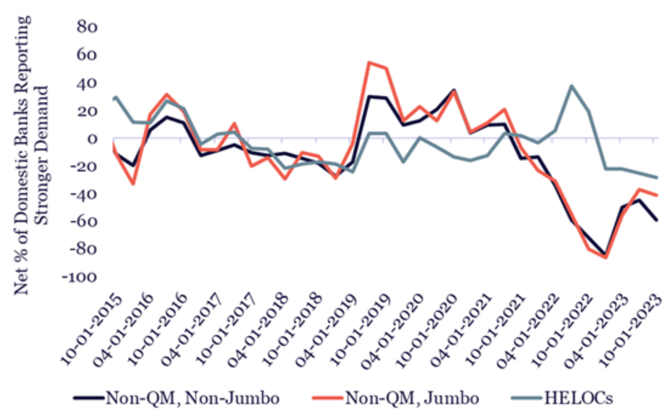
Housing Market Seesaw and Securitizations—Sales Down, Equity Up

In the third quarter of 2023, banks tightened lending standards for all categories of residential real estate loans and HELOCs amidst reduced demand, according to the October 2023 Senior Loan Officer Opinion Survey on Bank Lending Practices. The affected loan types include GSE-eligible loans, Qualified Mortgage (QM) non-jumbo non-GSE-eligible loans, QM jumbo loans, non-QM jumbo loans, non-QM non-jumbo loans, and subprime loans. This survey, which traditionally serves as a leading indicator of broader economic trends, suggests challenging times ahead. In a set of special questions, the Fed inquired about the reasons behind these tightened standards, with the most frequently cited reasons being economic concerns, reduced risk tolerance, and deteriorating credit quality.

U.S. Banks Are Offering Fewer Mortgage Loans...



...As Demand Drops

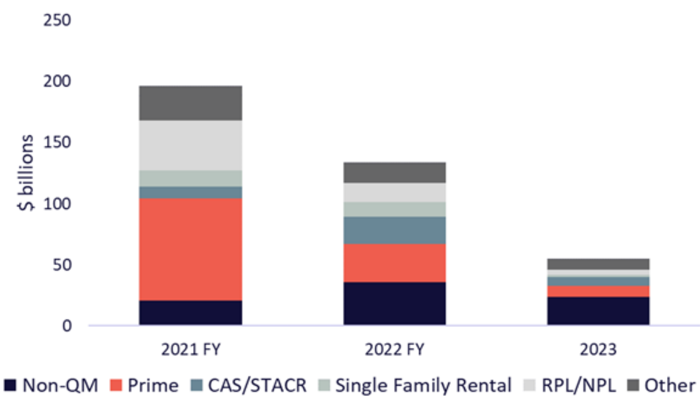


Source: Senior Loan Officer Opinion Survey on Bank Lending Practices

Tighter lending conditions is not the only thing weighing on the housing market. With mortgage rates nearing a 20-year high at 8% and record high housing prices, demand for mortgage loans has fallen. This is primarily because nearly three-quarters of homeowners are currently locked into mortgage rates of 4% or lower, as reported by ICE Mortgage Technology. While this can be a good thing for existing homeowners who are happy in their current homes, from a securitization perspective the prevalence of locked-in low rates and non-financial pandemic related factors disincentivizes owners from selling or refinancing their homes. This has had a significant impact on RMBS issuance as it has kept loan origination volumes depressed.

By the end of October, non-agency RMBS issuance reached $55 billion, 59% below 2022's total and 77% short 2021's full year volume, according to Deutsche Bank Research. The most substantial declines this year have been in RMBS backed by single-family rentals (down 79%), reperforming or non-performing loans (down 75%) and prime jumbo loans (down 70%). Fewer Credit Risk Transfer transactions have originated under the Fannie Mae (CAS)/Freddie Mac (STACR) platforms, which are down 69% from 2022. RMBS backed by non-qualifying (Non-QM) mortgages, making up 44% of the total non-agency RMBS volume this year, is down 32%.

Non-Agency RMBS Issuance 2021 to 2023 YTD

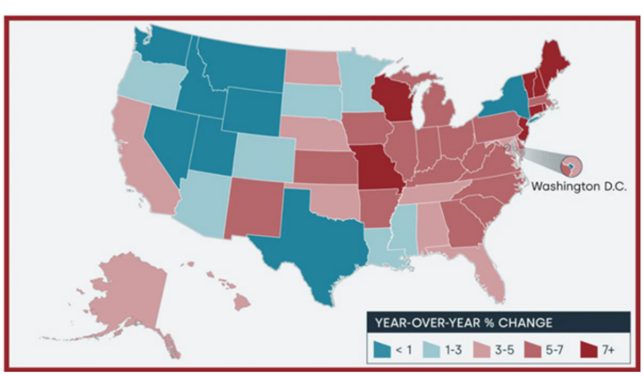


Source: Deutsche Bank Securitization Research, The Outlook

The flip side of soaring home prices is the substantial increase in home equity for existing homeowners, amounting to a collective $31 trillion, as reported by the Federal Reserve, equating to roughly $200,000 per homeowner. This development has also spilled over into RMBS. Notably, home equity-related collateral is a feature in 11 out of the 26 RMBS deals categorized as "Other." This category includes RMBS supported by both first and junior-lien revolving home equity lines of credit (HELOCs), home equity conversion mortgages (HECMs), commonly referred to as reverse mortgage loans, as well as a newcomer, home equity investments or agreements (HEIs or HEAs).

With home prices expected to continue to appreciate—[Corelogic HPI Forecasts] expects a 2.6% increase over the next year, following a 4.5% year over year increase recorded in September 2023—we would expect to see continued interest in home equity-related RMBS products in the market.

Year-over-year Home Price Changes by State, September 2023



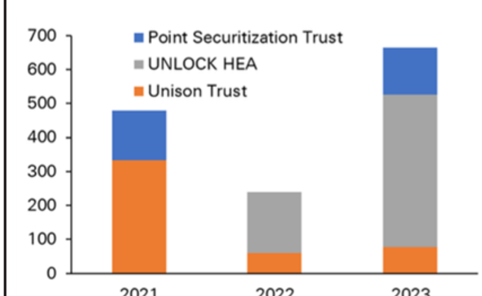
Source: CoreLogic HPI, National and State Maps, September 2023

Access to Equity Through Agreements

Unlike HELOCs or HECMs, HEIs are not loan products. [As non-recourse forward sale contracts], the HEI provider pays the homeowner a lump sum upfront cash payment in exchange for a share of the home's equity when the home is sold, refinanced, or purchased back by the homeowner. The payment amount is based mainly on the home's current equity; the future stake, which is a multiple of the current amount, is based on the home's future valuation and is subject to an annual cap. Unlike reverse mortgage loans, HEIs do not have a minimum age requirement. The HEI provider holds a junior security interest in the property, while the homeowner retains title, occupancy rights, and covers all taxes, maintenance, and expenses.

In 2021, Point with Redwood Trust issued the first HEI RMBS backed entirely by HEI agreements. Since then, the securitization market has provided funding for two other issuers Unison Trust and UNLOCK Technologies, with others, such as Hometap, [eyeing] the market. In October 2023, UNLOCK closed the first publicly rated securitization, the $224 million Unlock HEA Trust 2023-1. [DBRS Morningstar] rated the Class A BBB and the Class B, BB—credit protection for the bonds is provided by subordination. This deal was backed by 1,984 fixed HEIs secured by first, second, or third liens on residential properties in mostly California, Florida and Arizona, with original terms to maturity of up to 10 years. At closing, the HEI agreements in the pool reflected a contract to value of 19%. If the homes had existing mortgages, the combined contract and mortgage to value ratio was 57%.

HEI RMBS Issuance ($mn)



Source: Deutsche Bank Securitization Research, The Outlook, Introduction to HEI RMBS.