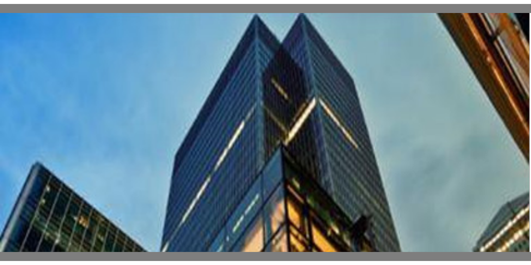
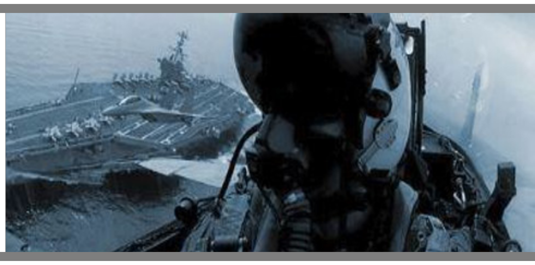
Housing at a Crossroads: Single-family and Multifamily Exposure Comparison





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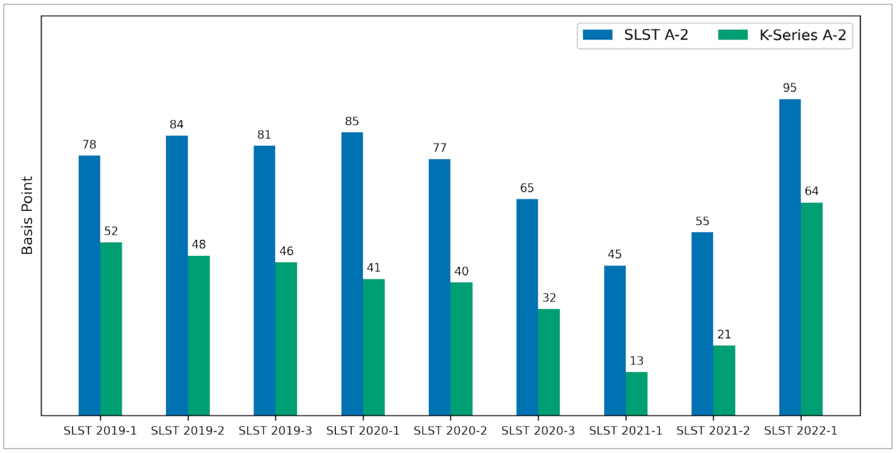
RPL, CRT, and Agency CMBS Provide Different Exposures to Housing Collateral

We expect a greater focus on the interplay between single-family and multifamily sectors as housing reaches a crossroads amid rising rate environment and post-pandemic supply/demand dynamics. Just released housing starts data underscore the potential different trajectories of the housing sectors. Single-family starts fell 7.3% in April to an annualized pace of 1.1 million units. In contrast, multifamily starts rose 15.3%.

Meanwhile, many homeowners are emerging from pandemic-driven forbearance and modifications. This highlights seasoned and re-performing pools as alternative housing exposure to newly originated mortgages. Forbearance loans have performed well compared to earlier "disaster" events, as we noted in a recent report.[1] For example, forbearance credit events across Freddie Mac's STACR credit risk transfers deals ("CRT") now hover around 1.67%, about two years following the disaster start date. This compares to 3.26-4.24% levels two years after Hurricanes Harvey and Florence, back in August 2017 and September 2018, respectively.

Agency re-performing single-family mortgage loans deals ("RPL") price wider to multifamily deals. Specifically, Freddie's most recent Seasoned Loans Structured Transaction ("SLST") priced its A-2 class last week at a spread of 95bp over the Treasury benchmark. This compares to a spread of 64bp on recent Freddie's K-series deals. SLST issuance spreads traded 26-44bp wider of K-series spreads over the past few years (Figure 1).

Figure 1. Freddie Mac SLST and Freddie K Spreads 2019-2022 (in basis points)



NOTE: Basis points shown are spread to UST on A2 class of respective SLST deal and generic K-Series A2 class the the time SLST was issued
Source: Bloomberg and Academy Securities

1 "Disaster Performance: Pandemic Forebearance Resolutions Bod Well for Future Stresses," CRT Credit Focus, Academy Securities, April 12, 2022

Low Delinquency Collateral

RPL, CRT, and agency CMBS all represent exposures to relatively strong collateral across securitized products. Multifamily delinquencies have been limited during the pandemic. The sector recorded 1.20% delinquency, as of April remittance, according to DBRS Morningstar. Pockets of weakness usually included niche multifamily segments such as student or senior housing.[2] Within RMBS re-performing and seasoned performing sector, overall 60-days or more delinquencies stood at 6.25% earlier this year, on average, down from a peak of 9.66%, according to Fitch. Both residential and multifamily seasoned mortgages stand to continue performing well in the near term. Homeowners with low in-place mortgage rates could show limited sensitivity to rising mortgage rates. In turn, multifamily landlords could adjust rents amid inflationary pressures on cost structures, thereby supporting their securitized mortgages. In Figure 2 we summarize some basic features of the three exposure types:

Figure 2. Simplified Comparison of Single-Family SCRT, CRT, and Multifamily Exposures

Agency CMBS	Credit Risk Transfer	Re-Performing Loans
• Multifamily exposure	• Single-family exposure	• Single-family exposure
• New Originations	• New Originations	• Seasoned mortgages
Performance Drivers:	Performance Drivers:	Performance Drivers:
• Underwriting standards	• Underwriting standards	• Payment histories
• Rent growth	• Prepayments	• Modification type
• Multifamily supply/demand dynamics	• Housing supply/demand dynamics	• Borrower current parameters

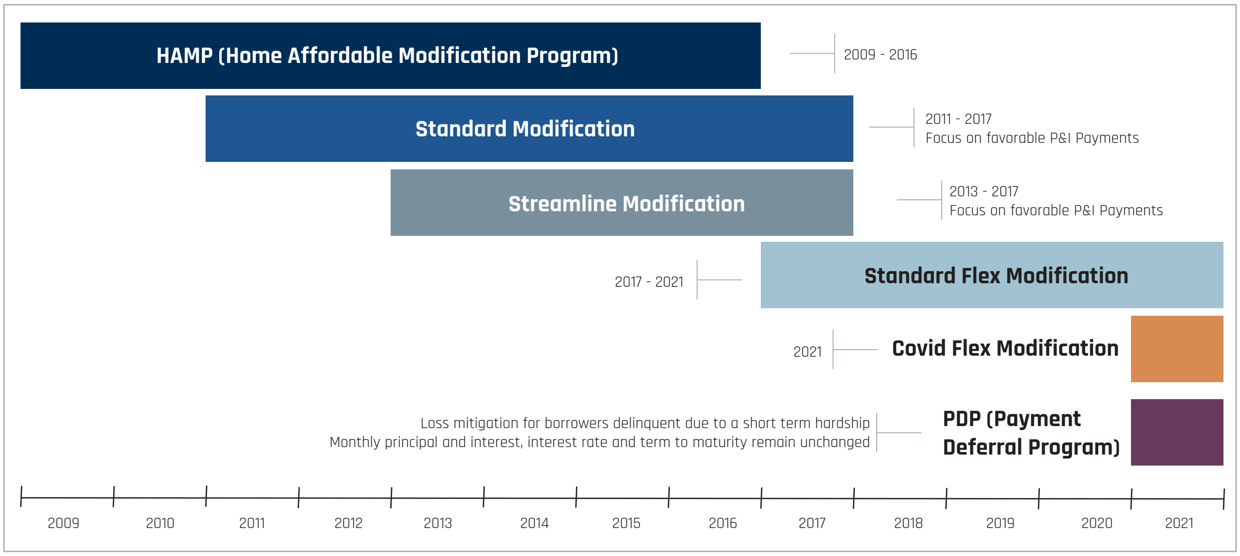
Source: GSE documents and Academy Securities

Modification Type Can Impact Re-performance Pattern

RPL exposure should also facilitate a view on different residential mortgage modification programs. Mortgage mods have evolved in recent years, potentially leading to varying re-performance patterns depending on the mod type. For example, modified mortgages that include a step-rate provision may have a greater risk of delinquency when the mortgage rate and associated monthly payment of the modified mortgage are increasing. Figure 3 summarizes the evolution. Figure 4 shows a breakdown of the modification types in SLST 2021-2.

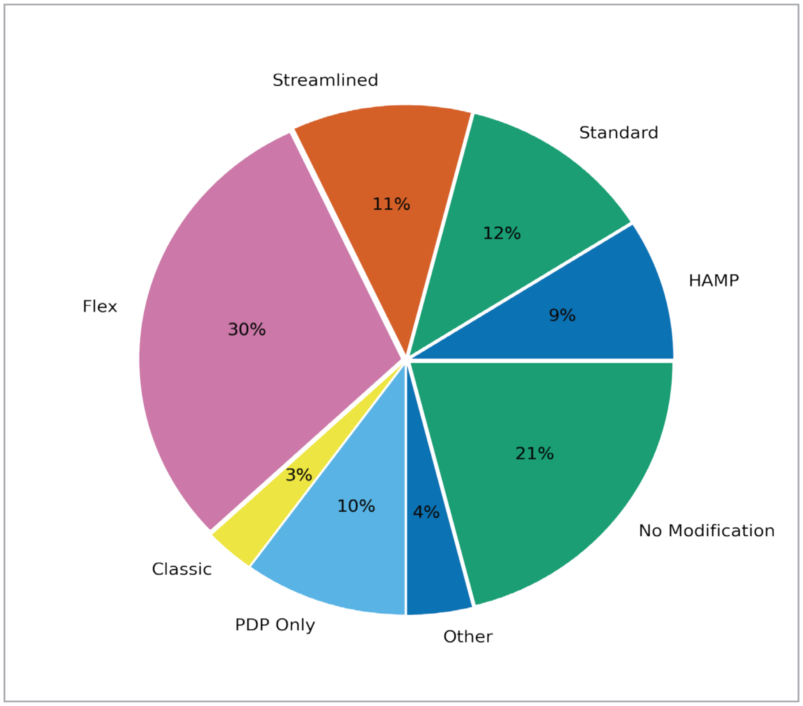
2 "Senior Housing: Focus on Secment Selection Amid Pandemic Impact," Securitized Products Special Topics, Academy Securities, May 3, 2022

Figure 3. GSE Modification Programs Timeline



Source: GSE documents and Academy Securities

Figure 4. SLST 2021-2 Pool by Modification Program

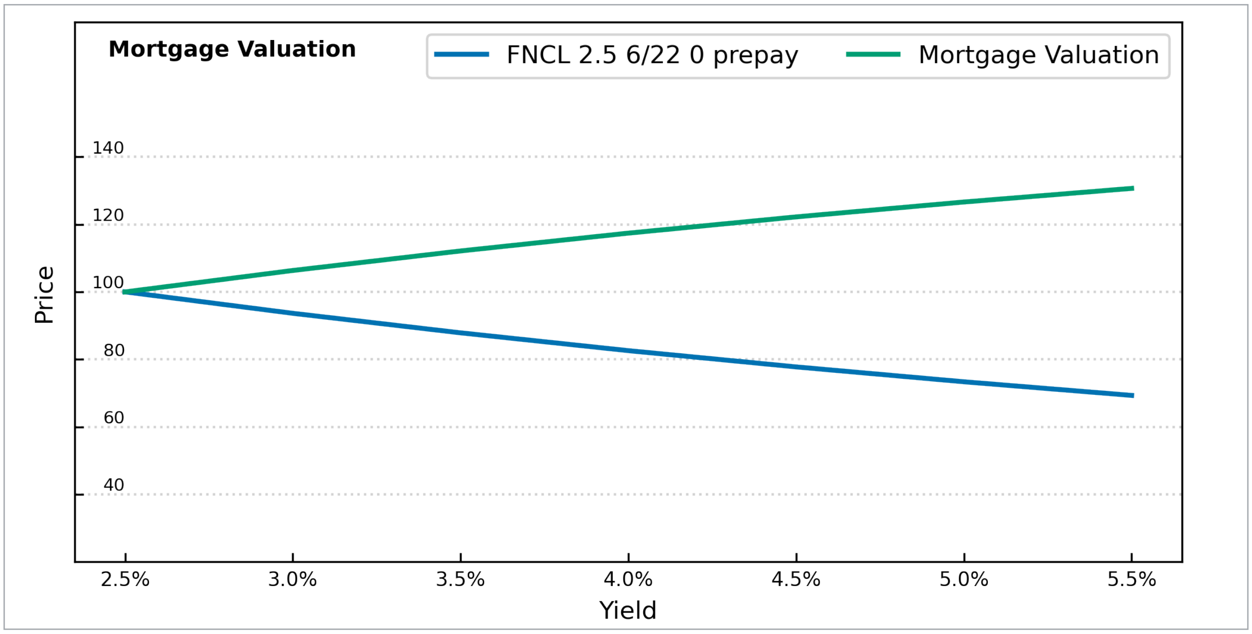


Source: Deal documents and Academy Securities

Seasoned Mortgages Value Amid Rising Rates

The reperforming mortgage market should benefit from embedded value driven by modifications and/or HPA. A simple modification scenario illustrates this. Assume a mortgage was modified in 2021 with a 2.5% APR and 30-year mortgage rate. The agency market can inform the value of such modified mortgage. FNCL 2.5 6/22 is the current 2.5% TBA market, currently trading at 91.72. As such, the homeowner's current 2.5% mortgage with 30-year maturity is valued roughly at 108.28. As rates continue to rise homeowners with modified mortgages are incentivized to avoid delinquencies or re-financing – the homeowners' payments are lower than what new mortgages would require. Figure 5 shows the valuation of a 2.5% APR mortgage with no prepayment.

Figure 5. Modified Mortgage Valuation Scenario



Source: Bloomberg and Academy Securities

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