Chapter 10

Residential Mortgage Loans

Mortgage

Conventional
Insured - FHA, VA, FmHA, PMI
Residential/Non-residential

Mortgage Originators

Original Lender - thrifts, commercial banks, mortgage bankers, life insurance companies and pension funds

Original lend profits

Origination fees
Secondary market profit
Held in mortgage portfolio

Lending factors

Payment-to-income ratio (PTI)
Loan-to-value ratio (LTV)

Lender can 1) hold mortgage in portfolio, 2) sell mortgage, or 3) use as collateral for issuance of a security (securitized)

Conduits - pool mortgages and sell them to investors

Federal Home Loan Mortgage Corp.
Federal National Mortgage Association

Conforming mortgages - max PTI, max LTV, max amount
Nonconforming
Mortgage Servicers
   Income - service fees, escrow interest, float, late fees, credit life

Mortgage Insurance
   PMI - private mortgage insurance - covers 20-25% of loan amount
   Credit life

Amortized mortgages
   Fully amortized

Adjustable Rate Mortgages
   Reference Rate
      Market determined
      Bank cost of funds - 11th district average cost of liabilities

Balloon Mortgages

Two-Step Mortgage
   Adjustable with one rate change

Prepayment Penalty
   Lockout period - period during which prepayments are limited

Growing Equity Mortgage

Reverse Mortgages
Risk Associated with Investing in Mortgages

Credit Risk
- Credit Risk - individual versus pooled
- Loan-to-Value Seasoning - LTV best indicator of likely default
  - Original versus current LTV
- Higher default rate for secondary financing
- Mortgage Term
- Mortgage Type - fixed versus adjustable
- Transaction Type - cashout riskier
- Documentation
- Occupancy Status
- Property Type - single versus multi-family
- Mortgage Size - large loans riskier
- Credit Worthiness of Borrower - information not available to raters

Liquidity Risk
- Secondary market - bid-ask spread

Interest-Rate Risk

Prepayment Risk