Common Securitization Platform: Making it work

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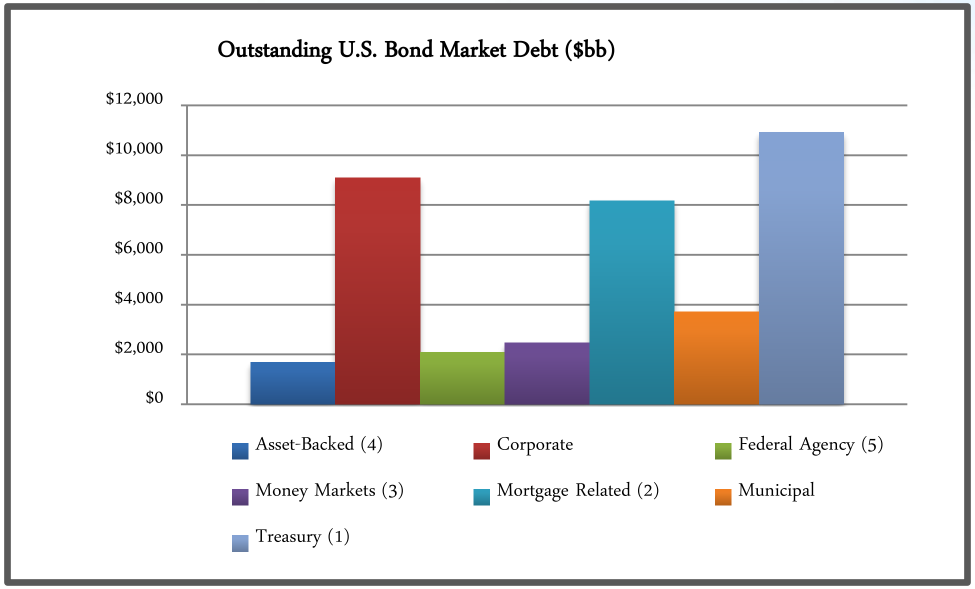
Common Securitization Platform

- Three critical policy decisions which will impact industry acceptance and participation in a common securitization platform
  - Transparency
  - Governance
  - TBA Market

Size of U.S. Securitized Debt



Source: SIFMA; data as of 2012-Q4

1 Interest bearing marketable public debt.
2 Includes GNMA, FNMA, and FHLMC MBS/CMOs; and private-label MBS/CMOs.
3 Includes commercial paper, bankers acceptances, and large time deposits.
4 Includes auto, credit card, home equity, manufacturing, student loans and other; CDOs of ABS are included
5 Contains agency debt of Fannie Mae, Freddie Mac, Farmer Mac, FHLB, the Farm Credit System, and federal budget agencies (e.g., TVA)

What distinguishes RMBS?

Treasury	
Corporate	
Municipal	
Federal Agency	Residential MBS
Money Market	
Asset-Backed	
Commercial MBS	

Strictly Private and Confidential

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Updated Disclosure on Collateral Quality

YES	NO
Treasury	Residential MBS
Corporate	Agency & Non-Agency
Municipal	
Federal Agency	
Money Market	
Asset-Backed *	
Commercial MBS	

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Disclosure and data transparency will be cornerstones to acceptance of CSP

- Ability to observe, model and manage risk will be elevated to new levels in CSP
- Most regulatory and legislative actions are focused on "issuance" disclosure, and the on-going disclosure of fields related to payment history and status.
  - Payment and status do not by themselves help identify causality
  - Data exists to help define causality—that should be focus
- Need updates to collateral (LTV) and borrower (balance sheet)
- Enterprises have not proven good stewards of this valuable (now arguably public) asset.
  - Created asymmetric information to leverage as guarantor
- Make more data available to market on consumer and losses, and they must be attributable to pools
- Massive amounts of model risk exist without the right data

Better disclosure from CSP will broaden credit risk distribution

- FHFA has done an outstanding job with origination standardization
  - UMDP (ULDD, UAD, UCDP), UMSD
- Securitization investors care about on-going data
  - Quality over quantity
  - Determinants of risk and reward
  - Big data is a big problem
- Technology advances are far ahead of Enterprises in ability to manage, protect and provide needed data
- Focus on dynamic elements that cause risk (Prepay, PD, LGD)
  - Collateral
  - Borrower
- CSP can help level playing field and improve best practices by being a forceful leader in expanding and enhancing data availability

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Risk Transfer

- First example in market of how FHFA/CSP would provide more data to securities investors
- Enterprises required to test market for cash or synthetic transactions to transfer credit risk.
- Mortgage credit is no longer a "buy and hold" asset—becomes transactional
- Cannot legislate or contract on every outcome—transparency allows people to make informed decisions
- Stated goal of risk transfer is reducing risk by "reducing the footprint"
- Risk transfer data released in recent weeks infer specific structure in mind
  - Creating structure which continues asymmetric data and information is not best first step for change
  - Private sector can provide valuable feedback loop which can enlighten future actions

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Preservation of the "Golden Egg"

- TBA market has been the single most important driver of depth of liquidity in single family RMBS
- Reality check! This isn't your Father' TBA market
  - TBA market is purely cheapest to deliver now
- Other markets are highly liquid
  - without TBA execution
  - much smaller size
- SEC exemptions appear to be the key to TBA efficiency
  - Enterprises/Government need not control or monopolize benefit
  - Exemptions can be provided to broader participants

TBA Market of the Future

- Risk exists to TBA future effectiveness due to:
  - Temporary investors dominating activity
  - Economic expansion will reduce refinance activity in 2015 and beyond
  - Cheapest to deliver is way beyond intent
    - In past it was a liquid market of the average delivery
    - Now it is a cesspool of garbage
    - Market pay-ups for specified pools indicate extent of mutation
- Benefits of Enterprises as sole-sponsors of TBA market have diminished
- Common platform should orchestrate ability of non-GSE delivery into TBA market
  - Requires standardization and governance
- CSP, not Enterprise modernization, is best outcome for future market

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Governance of CSP

- Governance exists to ensure separation of powers and duties
- Institutions that insure risk should not control the dissemination of data to the public.
  - Natural conflict of interest
  - Empirical challenges as proof
- Industry will not broadly accept market where data is controlled by guarantor of risk
- CSP can ensure that standards are consistent with industry needs while still maintaining flexibility needed to react to changes
- Naming of CEO of new third platform should be an eye-opener for Enterprises

Summary

- CSP is a well thought out concept with many outstanding decisions
- Transparency and data disclosure is paramount issue for CSP success
- Risk transfer transactions need to be more literal relative to “spirit” of “reducing the footprint”
- Liquid mortgage markets (TBA) don’t require one of the existing Enterprises to be successful
- Governance must cultivate adequate separation of duties and broaden industry inclusion