Yield Book Mortgage Research

Responsible Lending behavior metrics and scores: Outsized Rates

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Responsible behavior in a lending context is the practice of extending fair and reasonable terms to borrowers during the loan origination process; to facilitate the measurement of and highlight the extent of potentially predatory practices within a deal or market segment, quantitative-based metrics have been developed.

Loans issued and then passed to the three different Government Sponsored Enterprises (GSEs) (GNMA, FNMA, and FHLMC) have been considered as separate universes, due to the different eligibility requirements. In this research, we focus on 30 Year Fixed Rate Loans originated after the Great Financial Crisis (GFC).

Overview of Methodology

The Yield Book mortgage prepayment model has been accepted as the golden standard for projecting borrower payment behavior for decades. Within that framework, we have developed the ability to closely predict an expected mortgage rate for a borrower with given characteristics (FICO, LTV, DTI, and others) at each point in time. For each lender, we compute the difference of the actual loan rate from the expected loan rate over that lender's loan production. This metric is commonly referred to as SATO – Spread at Origination.

We quantify High-Rate Lending as systematic deviation of a lender's loan production vs typical loan production. In the chart below, we show the overall spread for all loans in consideration. The distribution is nearly symmetric and heavily concentrated around zero.

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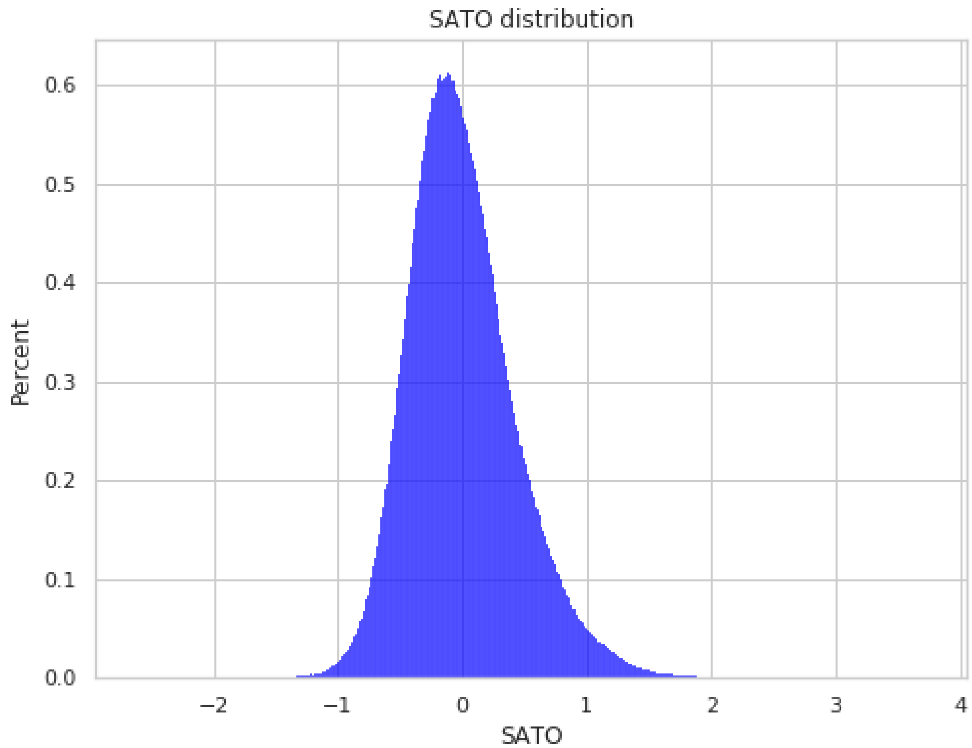
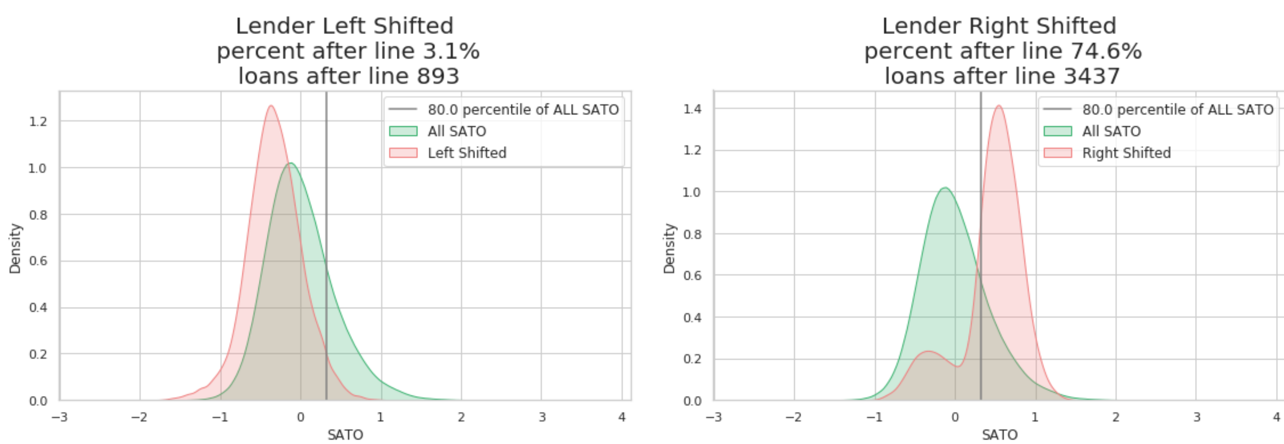
Figure 1



Source: Yield Book

By no fault or predatory intentions, some of the lender's production will fall to the right side of zero indicating the actual rate is higher than the predicted rate. However, when a significant portion of a lender's production falls to the right side, this indicates significant evidence of systematic lending at rates above what can be justified by borrower characteristics or market conditions. Alternatively, a significant percentage of production below zero indicates a positive tilt showcasing lenders subsidizing borrowers in the marketplace. The plot below shows examples of both. The green curve shows the global distribution.

Figure 2



Source: Yield Book

Results

In the three tables below we show the top 5 lenders ordered from most right skewed from typical lender production first. The results are presented for lenders selling into GNMA FHA, FNMA, and FHLMC.

Table 1. GNMA FHA table

Lender	Loan Production	% More than 80th Percentile	LSEG Deviation Score
1S*****	308	74%	1.74
AM*****	8229	54%	1.54
PR*****	2353	48%	1.48
KE*****	665	47%	1.47
SU*****	728	43%	1.43

Source: Yield Book

Table 2. FNMA table

Lender	Loan Production	% More than 80th Percentile	LSEG Deviation Score
UT*****	5553	100%	2.00
KE*****	8262	95%	1.95
MI*****	3487	88%	1.88
SE*****	1281	85%	1.85
CO*****	1141	77%	1.77

Source: Yield Book

Table 3. FHLMC table

Lender	Loan Production	% More than 80th Percentile	LSEG Deviation Score
UT*****	523	100%	2.00
GE*****	272	85%	1.85
CO*****	1444	71%	1.71
RP*****	2934	68%	1.68
AL*****	759	67%	1.67

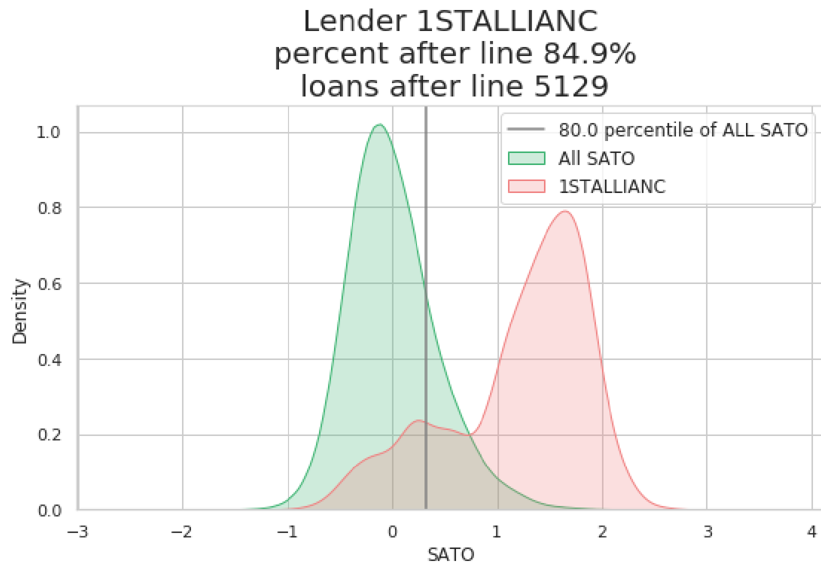
Source: Yield Book

This scoring methodology enables computing exposure at any level of aggregation. We focus on ranking lenders here. It is a straightforward extension to evaluate individual security exposure to lenders and create a ranking of securities with a high exposure to High-Rate lenders.

Related CFPB Action

It is worth mentioning that we **have not** incorporated data or information collected from the Consumer Finance Protection Bureau (CFPB) into our approach. The CFPB is the primary regulatory agency charged with protecting consumers from unlawful or predatory lending practices. When we look at lenders which we would characterize as High-Rate Lenders, we have found several examples of accusations of unlawful lending practices. In one particularly egregious example, we see rates for 1st Alliance Lending are heavily skewed and the CFPB has brought about legal action for unlawful lending practices.

Figure 3. 1st Alliance through the Yield Book High-Rate analysis:



Source: Yield Book

Figure 4.

Consumer Financial Protection Bureau Sues 1st Alliance Lending, LLC and Its Principals for Alleged Unlawful Mortgage Lending Practices

JAN 15, 2021

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WASHINGTON, D.C. – Today, the Consumer Financial Protection Bureau (Bureau) filed a lawsuit against 1st Alliance Lending, LLC, John Christopher DiIorio, Kevin Robert St. Lawrence, and Socrates Aramburu for allegedly engaging in various unlawful mortgage-lending practices. 1st Alliance, based in Hartford, Connecticut, originated residential mortgages from 2004 to September 2019 and stopped operating in November 2019. DiIorio was its chief executive officer and he, St. Lawrence, and Aramburu were 1st Alliance's three managing executives. The Bureau alleges that 1st Alliance, with DiIorio's, St. Lawrence's, and Aramburu's participation, knowledge, and direction, violated the Truth in Lending Act (TILA), the Fair Credit Reporting Act (FCRA), the Equal Credit Opportunity Act (ECOA), the Mortgage Acts and Practices–Advertising Rule (MAP Rule), and the Consumer Financial Protection Act of 2010 (CFPA). The Bureau's complaint, which was filed in the United States District Court for the District of Connecticut, seeks injunctions against the defendants, as well as damages, redress to consumers, disgorgement of ill-gotten gains, and the imposition of civil money penalties.

Source: Consumer Financial Protection Bureau Sues 1st Alliance Lending, LLC and Its Principals for Alleged Unlawful Mortgage Lending Practices | Consumer Financial Protection Bureau (consumerfinance.gov)

So far, we have not identified a lender with left skewed / measured market subsidizing rates that has been criticized by the CFPB, i.e. no false positives.

By the time the CFPB has adequate consumer complaints or uncovered unlawful / predatory practices, the behavior is widespread and the impact on consumer well-being is substantial. Utilizing Yield Book's scores gives market participants the opportunity to be proactive and avoid patronizing or supporting High Rate lenders.

About Yield Book

Yield Book is a trusted and authoritative source for fixed income analytics that enables market makers and institutional investors to perform complex analysis of their portfolios, benchmarks, trading decisions, historical performance, and risk. Yield Book products offer analytical insight into an extensive range of financial products in the fixed income space including governments, agencies, corporates, high yield, emerging markets, mortgages, ABS, CMBS, CMOs, and derivatives. The platform utilizes dedicated centralized servers that help ensure reliable, prompt data delivery. Yield Book forms part of London Stock Exchange Group's Information Services Division, which includes FTSE Russell, a global leader in indexes.

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