

THE HFA INSTITUTE 2024

Housing and Bond Market Updates for the New Year



National Council of State Housing Agencies



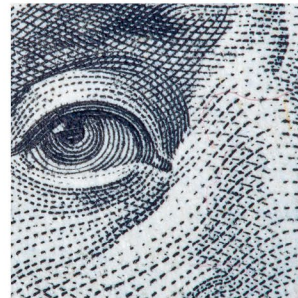
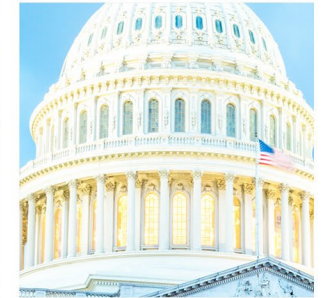
MRBs and Other Federal Homeownership Programs
JANUARY 10 – 12



Housing Credit
JANUARY 9 – 11



Section 8 and Other Federal Multifamily Programs
JANUARY 10 – 12



HOME and Housing Trust Fund
JANUARY 7 – 9



DISCUSSION LEADER

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Macro and Housing Outlook 2024: Housing Down Amid Affordability Pressures

Hamilton Fout

Economic & Strategic Research

Fannie Mae

January 10, 2024



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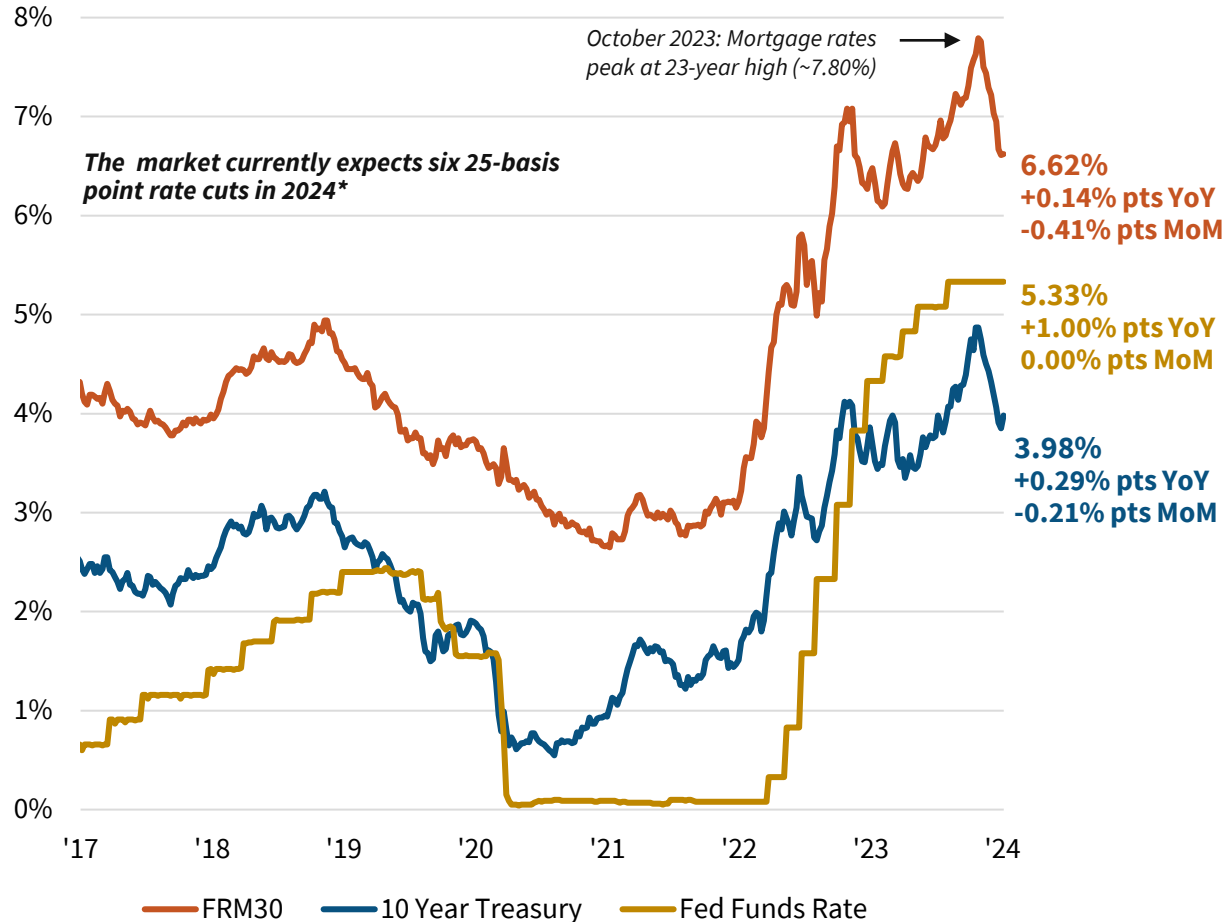


Macroeconomic Outlook

Mortgage rates come down from 23-year high

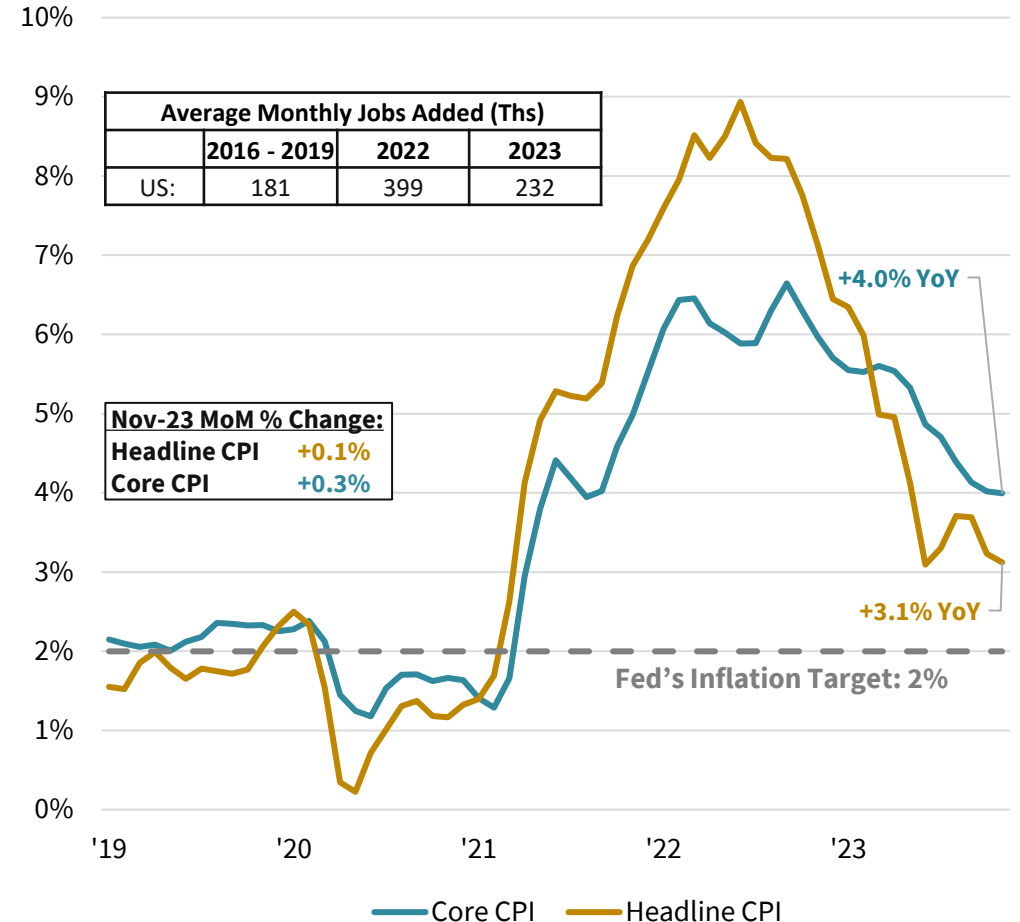
Inflation rate down from 2022 peak but remains above Fed 2% target

Weekly Interest Rates



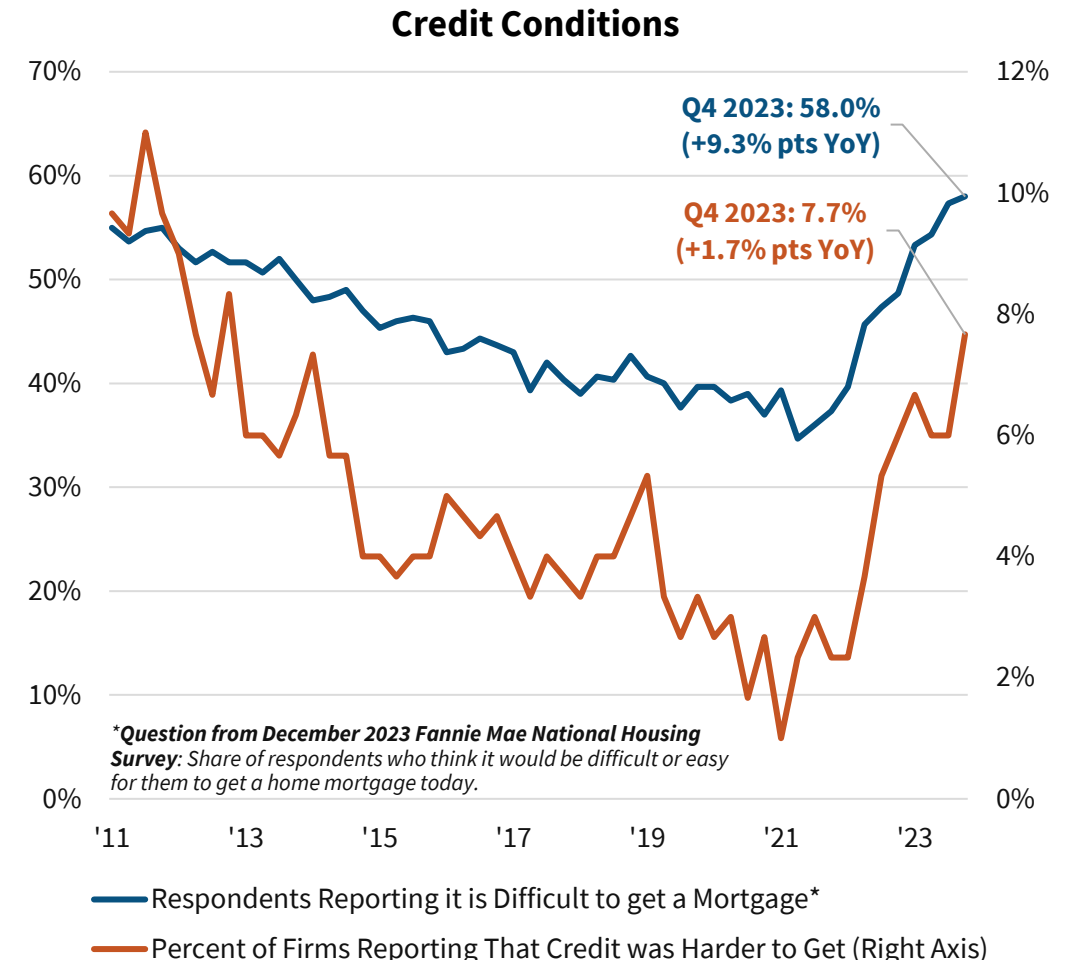
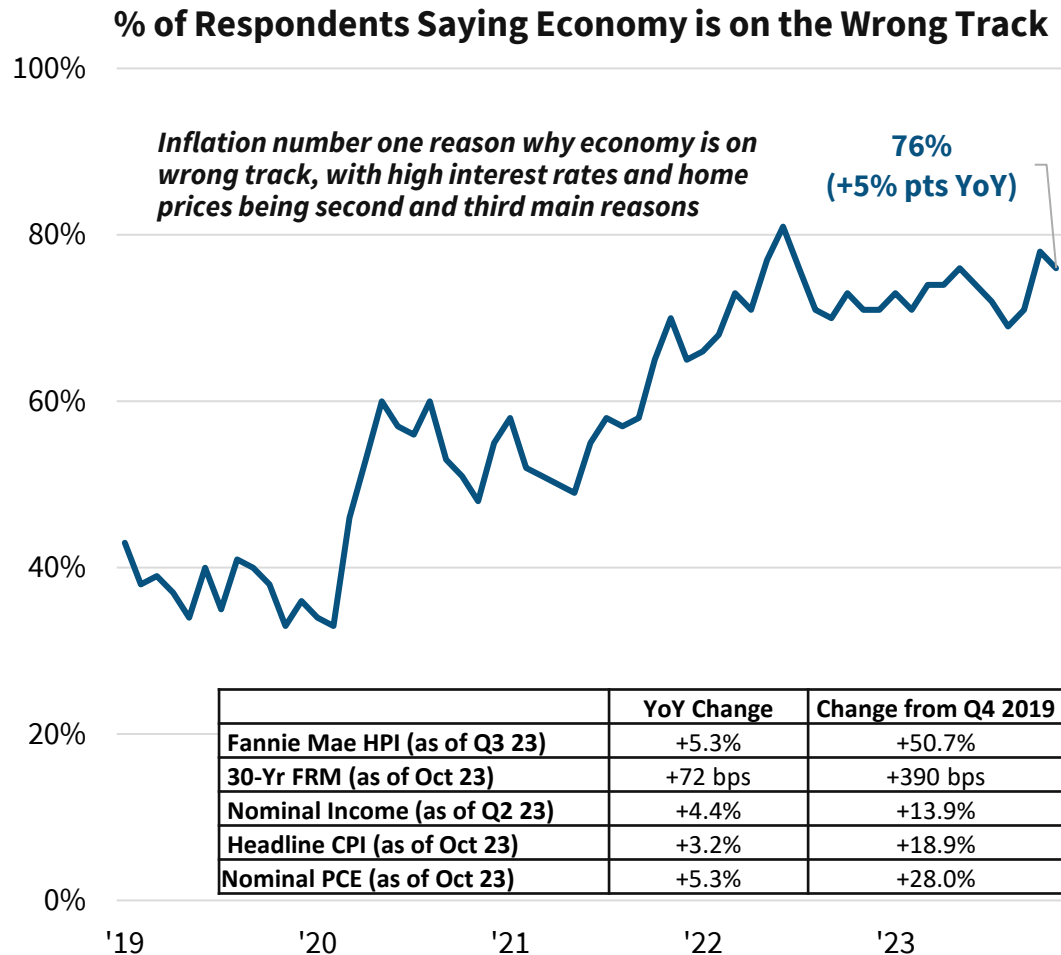
*as of 1/9/2024, 5:30 PM

YoY % Change in CPI



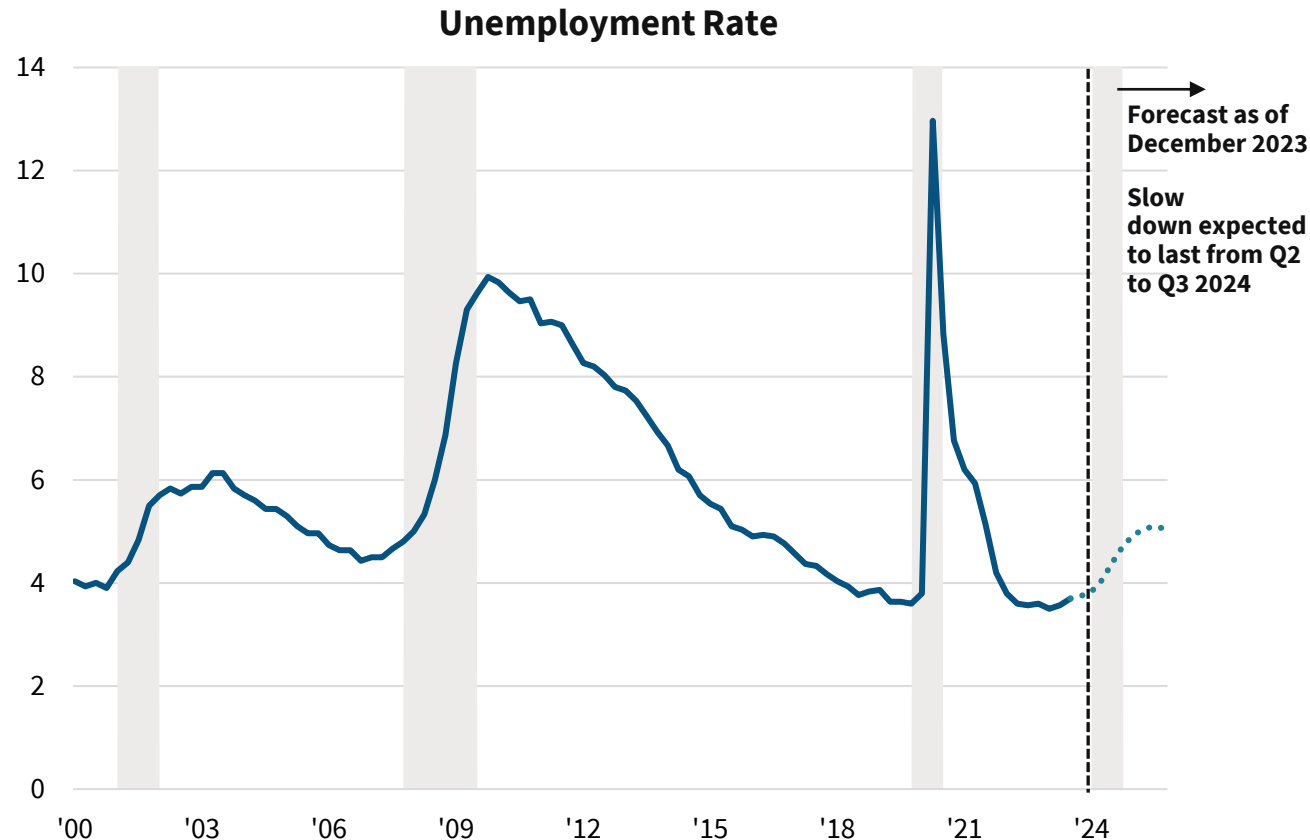
Households indicate pessimism about the economy

Higher prices and tighter credit conditions present risks to economic growth



Economic slow down expected in 2024 with recovery into 2025

Unemployment rate expected to increase and housing expected to remain sluggish for the year



2024 Outlook

- ❖ **Economy Contracts/Labor Market Weakens**
 - Unemployment rate to increase to 4.7% by Q4 2024
- ❖ **Consumption/Spending Slows**
 - Real consumption to decline by an annualized rate of 1.2% in 2024 Q2 and 0.5% in 2024 Q3
- ❖ **Home Sales Remain Weak**
 - 2024 total homes sales flat versus 2023 but down 30% versus 2021
- ❖ **Home Prices Soften**
 - Home prices to decelerate throughout 2024 with annual growth of 2.8% in 2024
- ❖ **Inflation and Long-term Rates Decline**
 - Headline CPI to decelerate to 2.1% YoY in 2024 Q4 as mortgage rates decrease to 6.5% by the end of 2024
- ❖ **Housing Affordability Improves**
 - Mortgage and interest payment for homebuyers expected to drop to 27% of income (versus 32% in Q4 2022) by the end of 2024

2025 and Beyond: Economic and labor market recovery along with improving affordability lead to a recovery in home sales and home prices

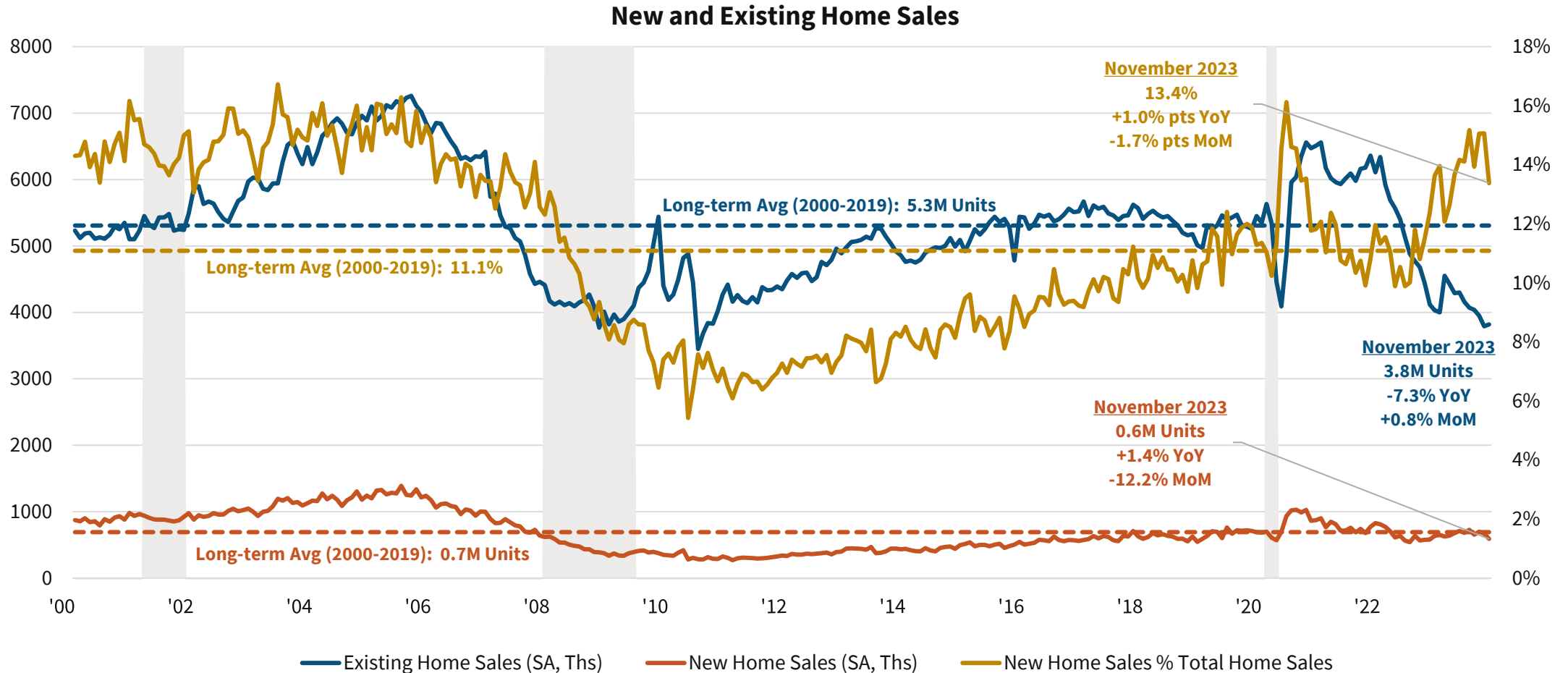




Single-Family Housing and Mortgage Markets

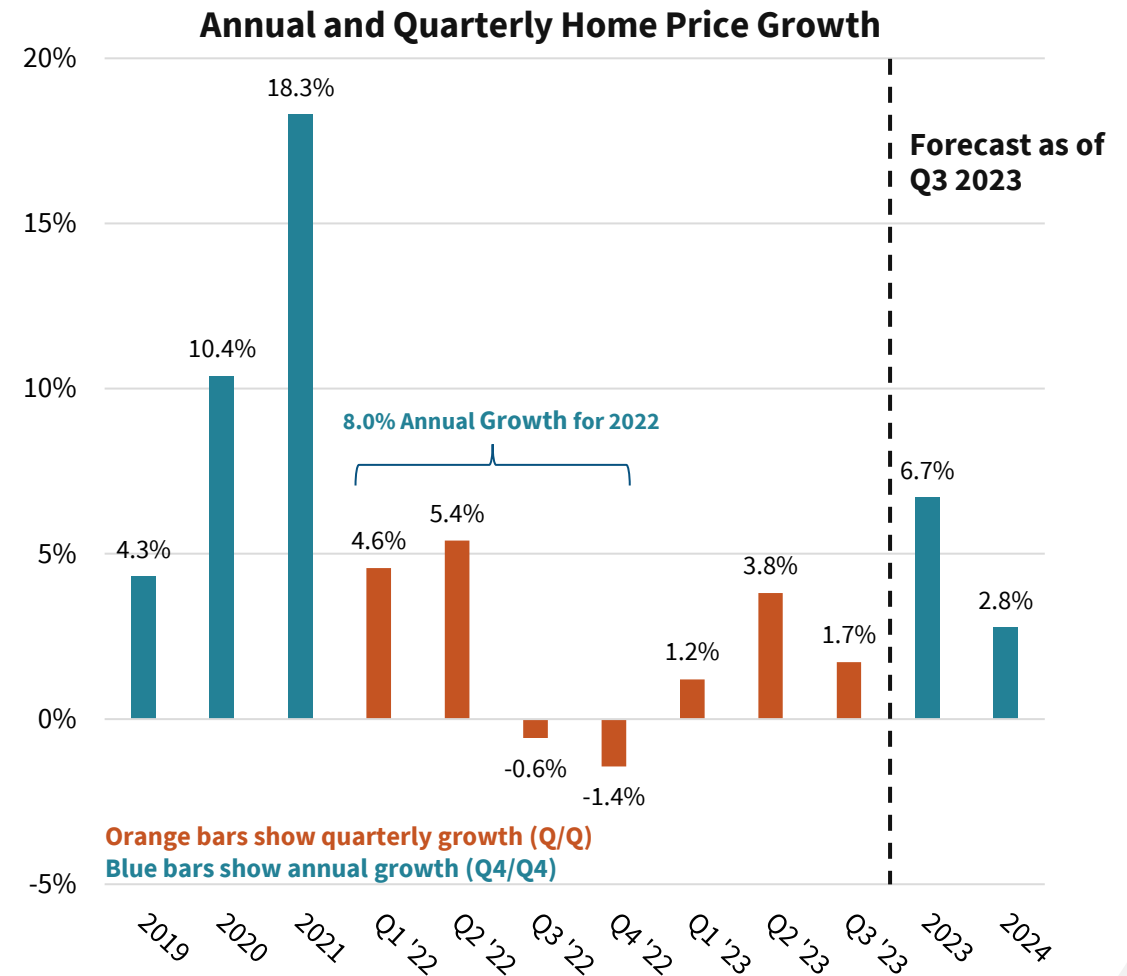
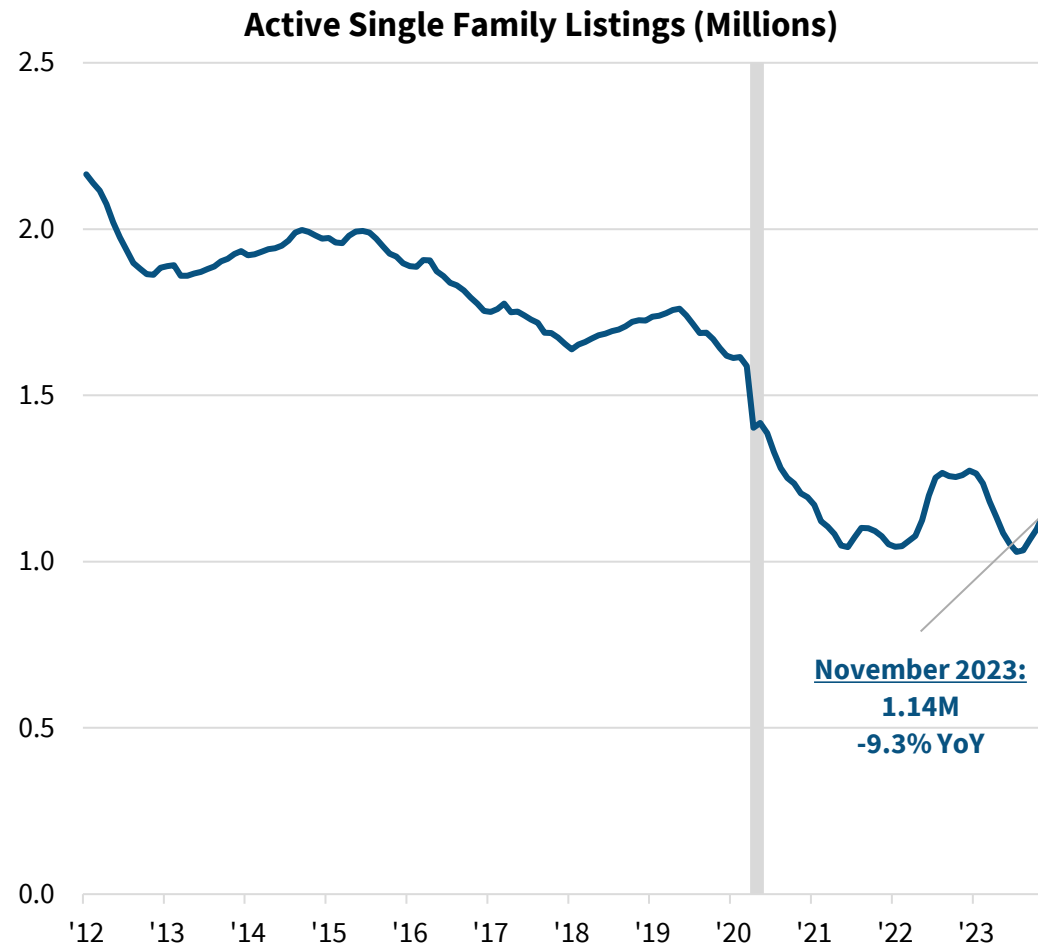
Existing sales remain at multi-year lows

Share of sales that are new homes rises above long-run average



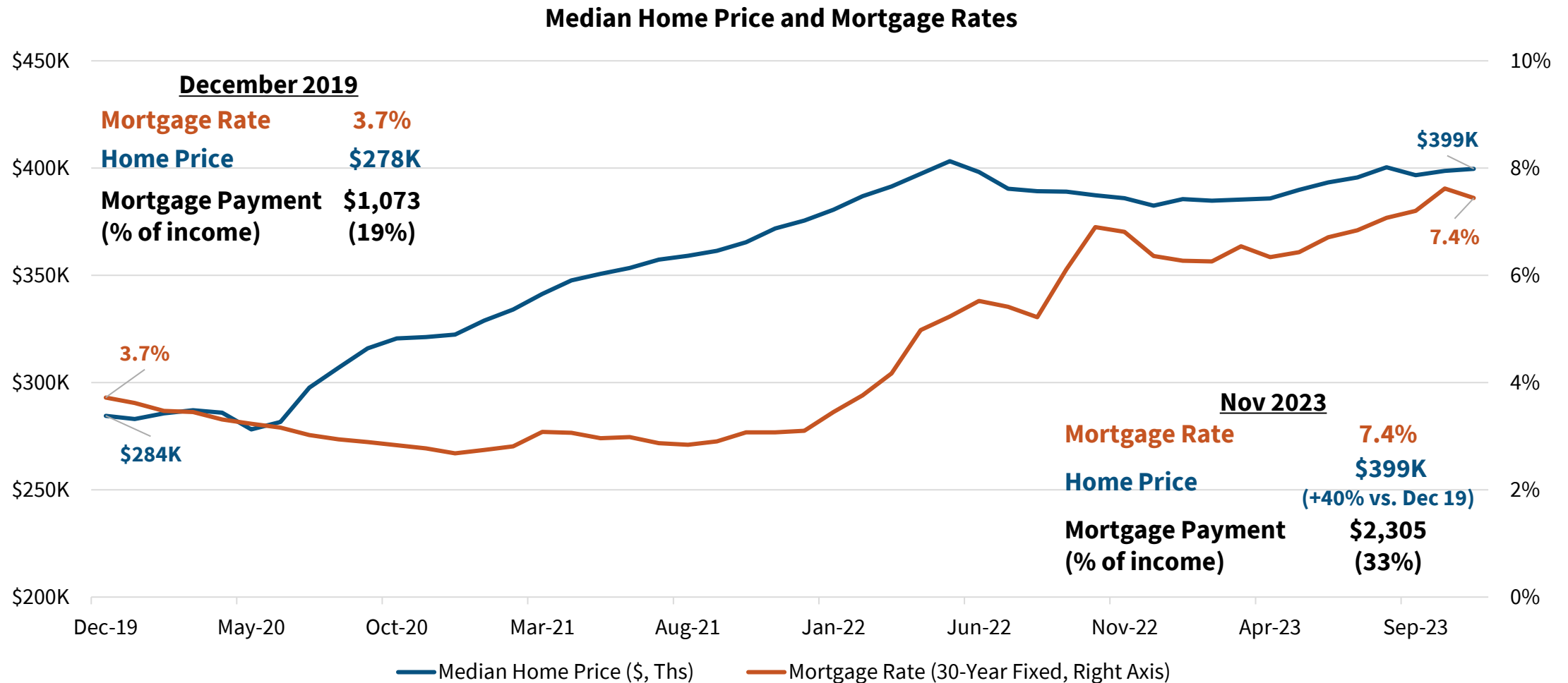
Limited supply continues to drive home price growth

Sales remain limited as homeowners remain reluctant to sell their homes



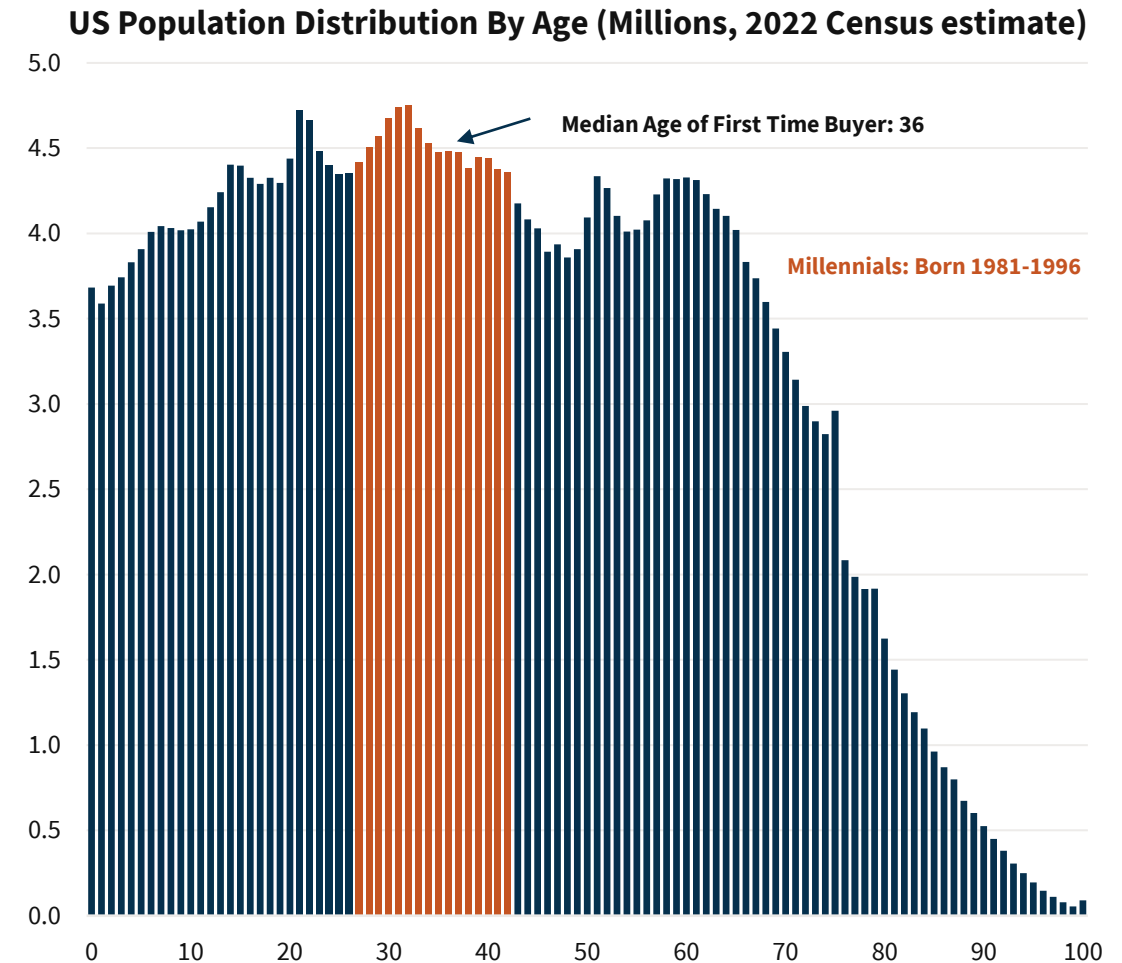
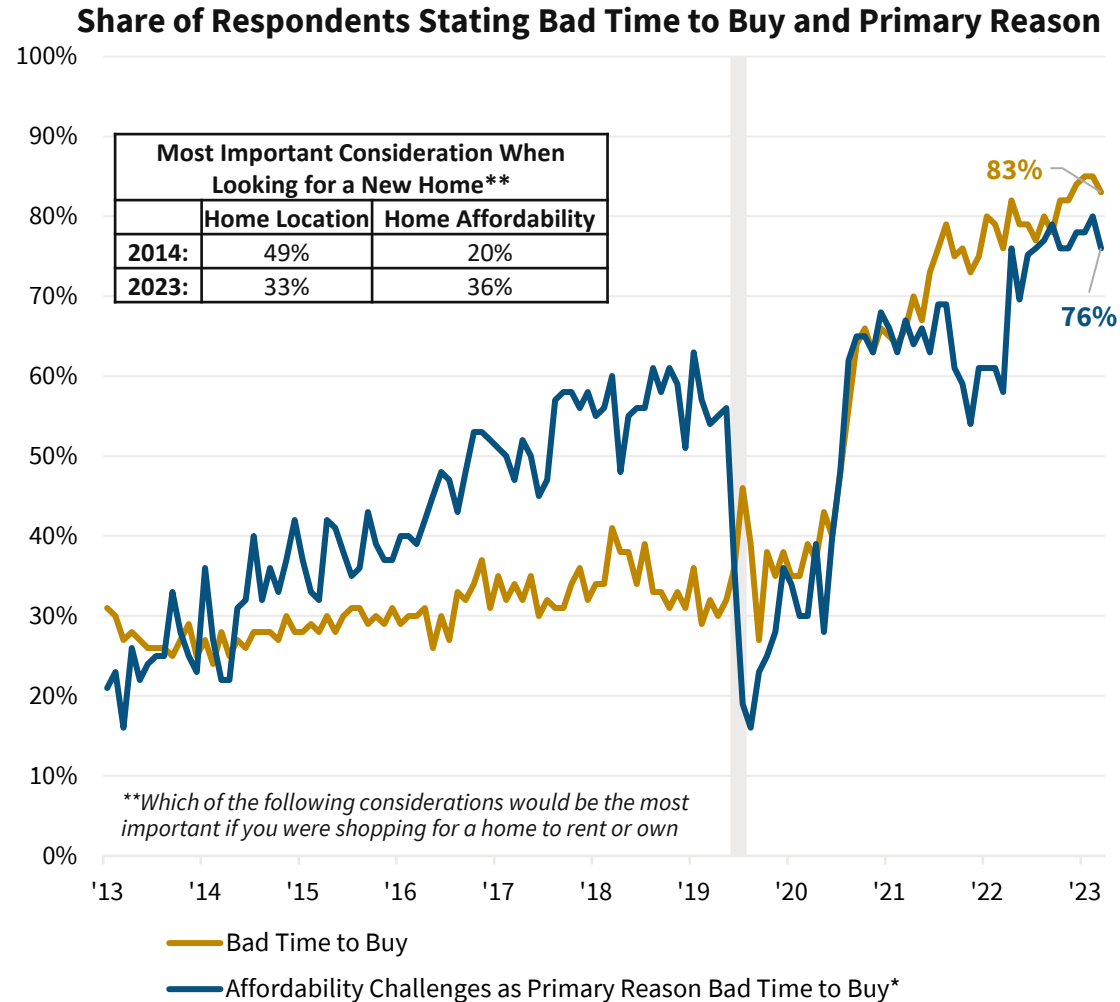
Home prices have grown by around 40% since 2019

Mortgage rates have more than doubled since the end of 2021



Households remain pessimistic about home buying given affordability challenges

Households indicate higher mortgage rates and home prices are primary challenges to buying



**Either high home prices or high interest rates as primary reason*

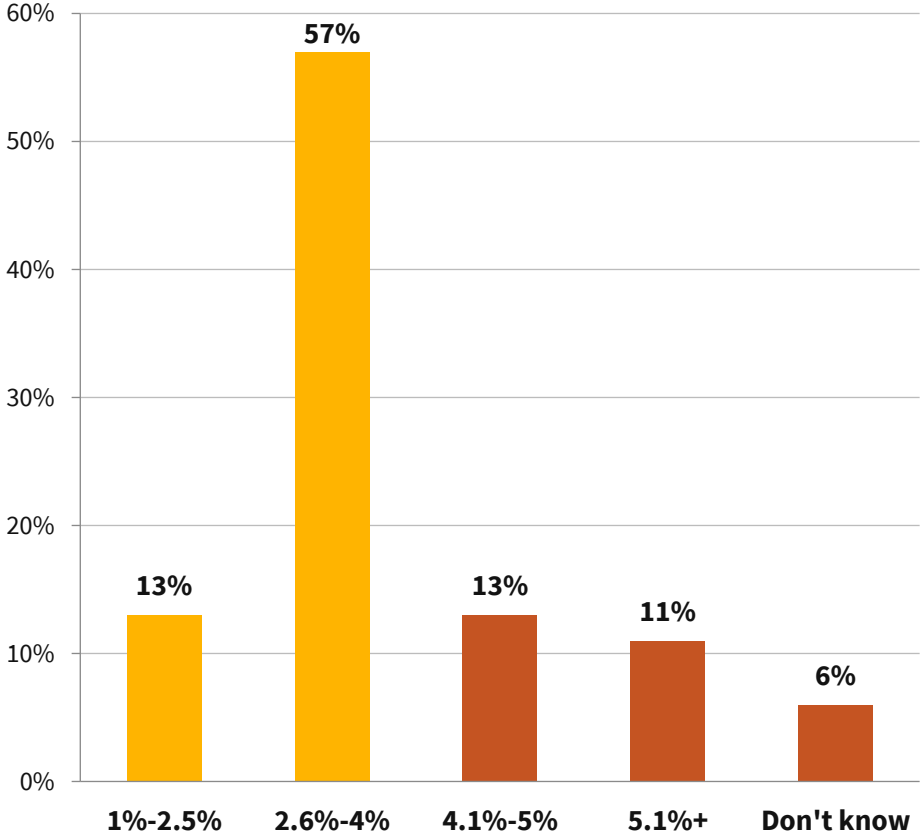


About 70% of borrowers said they have a mortgage rate of 4% or less

Mortgage borrowers are not selling because of rate lock in and because they are in the homes they want

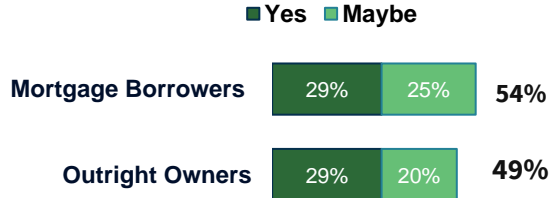
Mortgage Rate Distribution

Among Mortgage Borrowers in Q1 2023, n=1,199



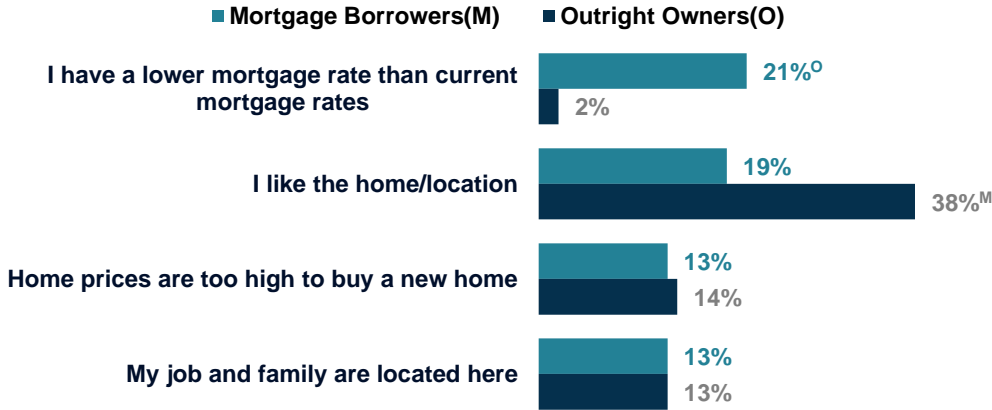
Q533: What is your home's approximate mortgage rate?

Will you stay in your home longer than you originally planned?



Top Primary Reasons for Staying in their Home Longer

Among Homeowners who said "yes" they plan stay in their home longer, ranked by Mortgage Borrowers



M/O: Denotes a % is significantly higher than the segment that the letter represents at the 95% confidence level within the quarter

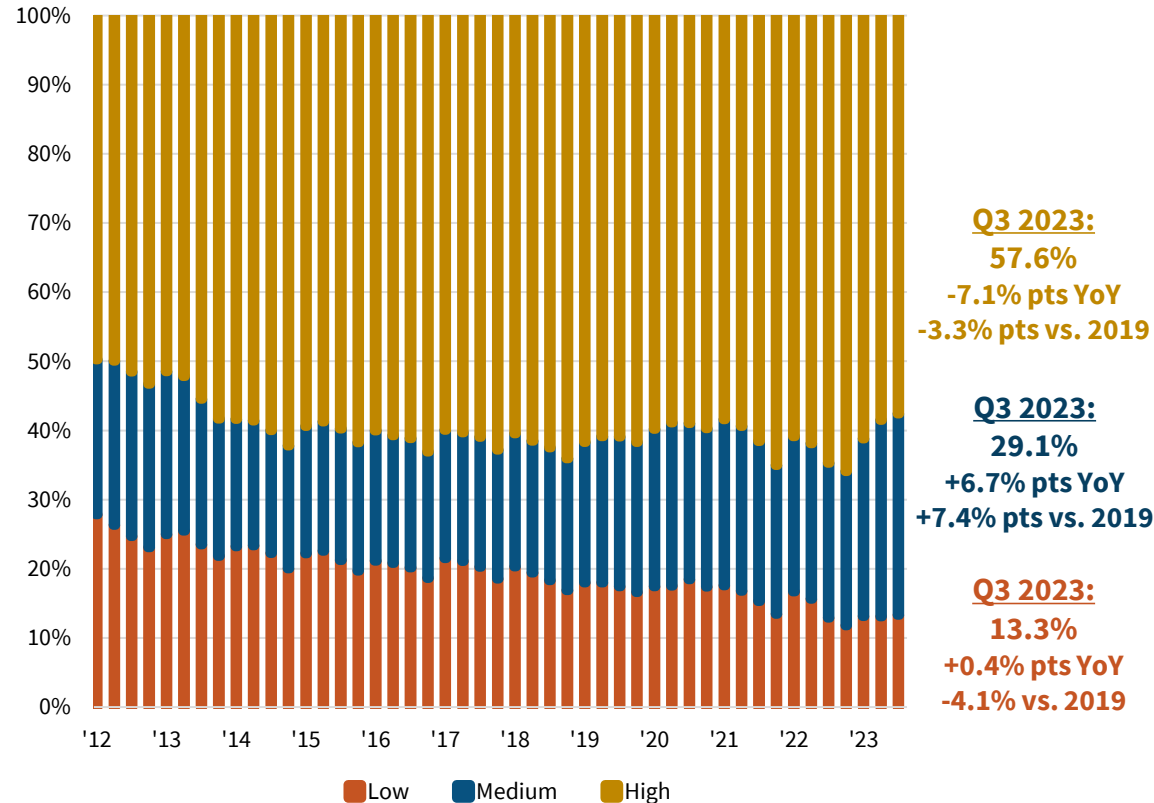
Q532: What are the reasons why you plan to stay in your current home for longer than you originally intended? (Primary Reason)
Percentage values across answer choices within each category may not always total to 100% due to rounding.



Home price construction remains concentrated at higher price tiers

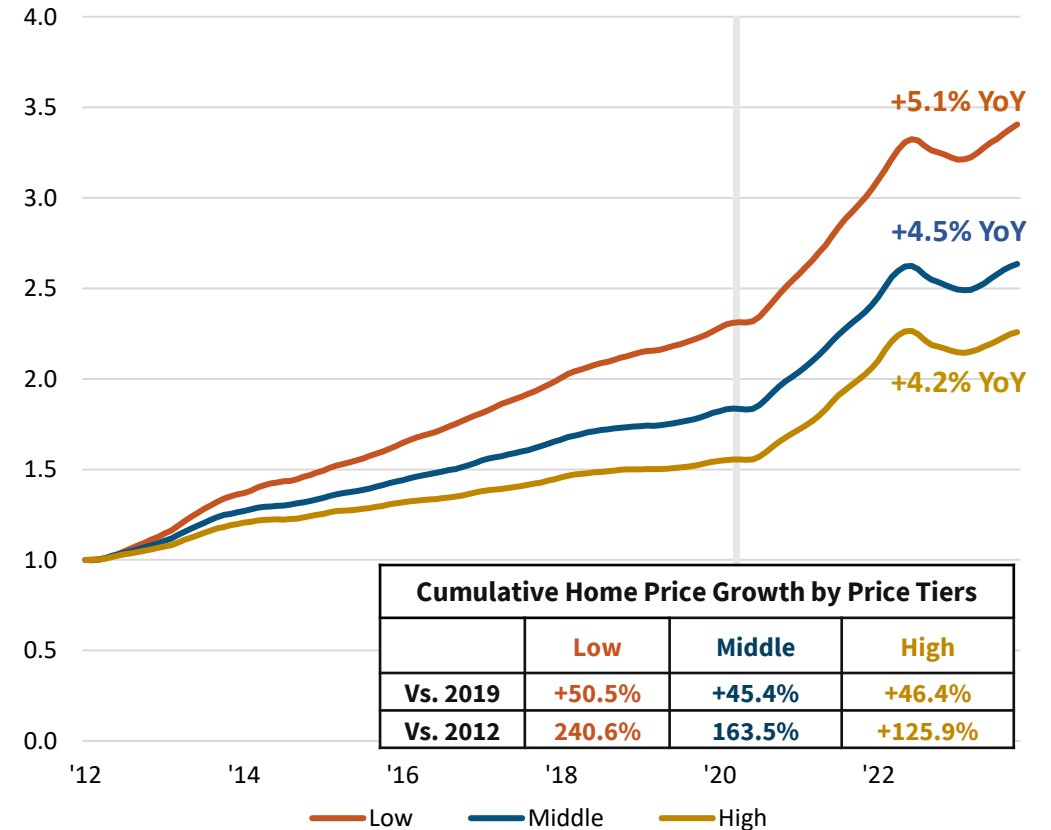
Home price growth in lower price tiers continues to outpace more expensive segments, given limited supply

Share of New Home Construction by Price Tier



Price Tier Methodology	
Low	All sales at or below the 40th percentile of FHA sales prices
Medium	All sales at or below the 80th percentile of FHA sales prices
High	All other sales

Cumulative Home Price Growth by Tiers (Jan 2012 = 1)

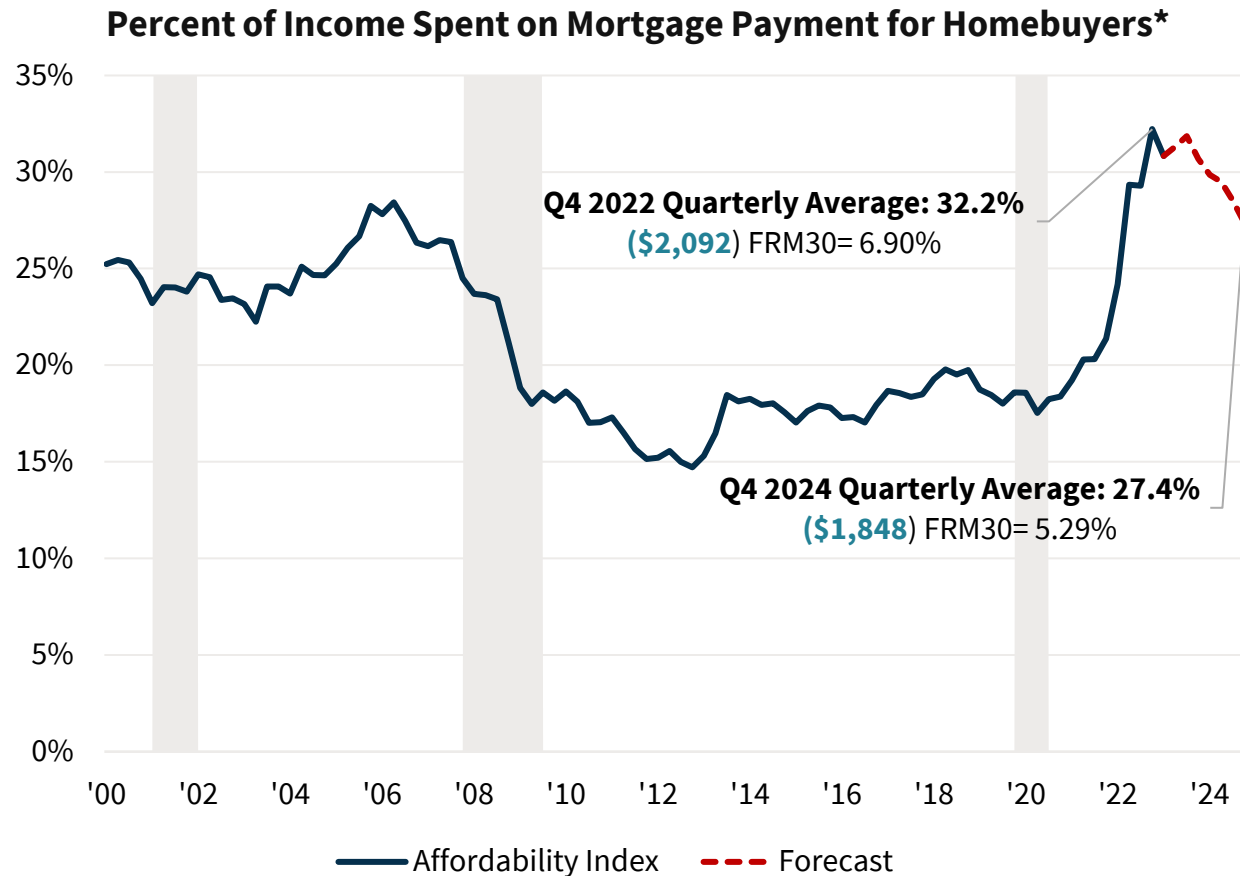


Price Tier Methodology	
Low	All sales at or below the bottom third of final sales price
Middle	All sales at or below the middle third of final sales price
High	All other sales



Affordability expected to improve over time

Home price growth softening, rate declines, and income growth could drive potential improvements



*Assumes 20% down payment, average 30-yr fixed-rate mortgage, median existing sales price, nominal median household income. Average monthly payments in parentheses.

- **Inflation declines** expected through 2024 **-0.4% pts****
- **Mortgage rate declines** expected through 2024 **-1.2% pts**
- **Home price growth slows** in 2024 **+2.8%*****
- **Nominal income growth** expected through 2024 **+3.0%****
- **Existing home sale rise** expected through 2024 **+5.3%****

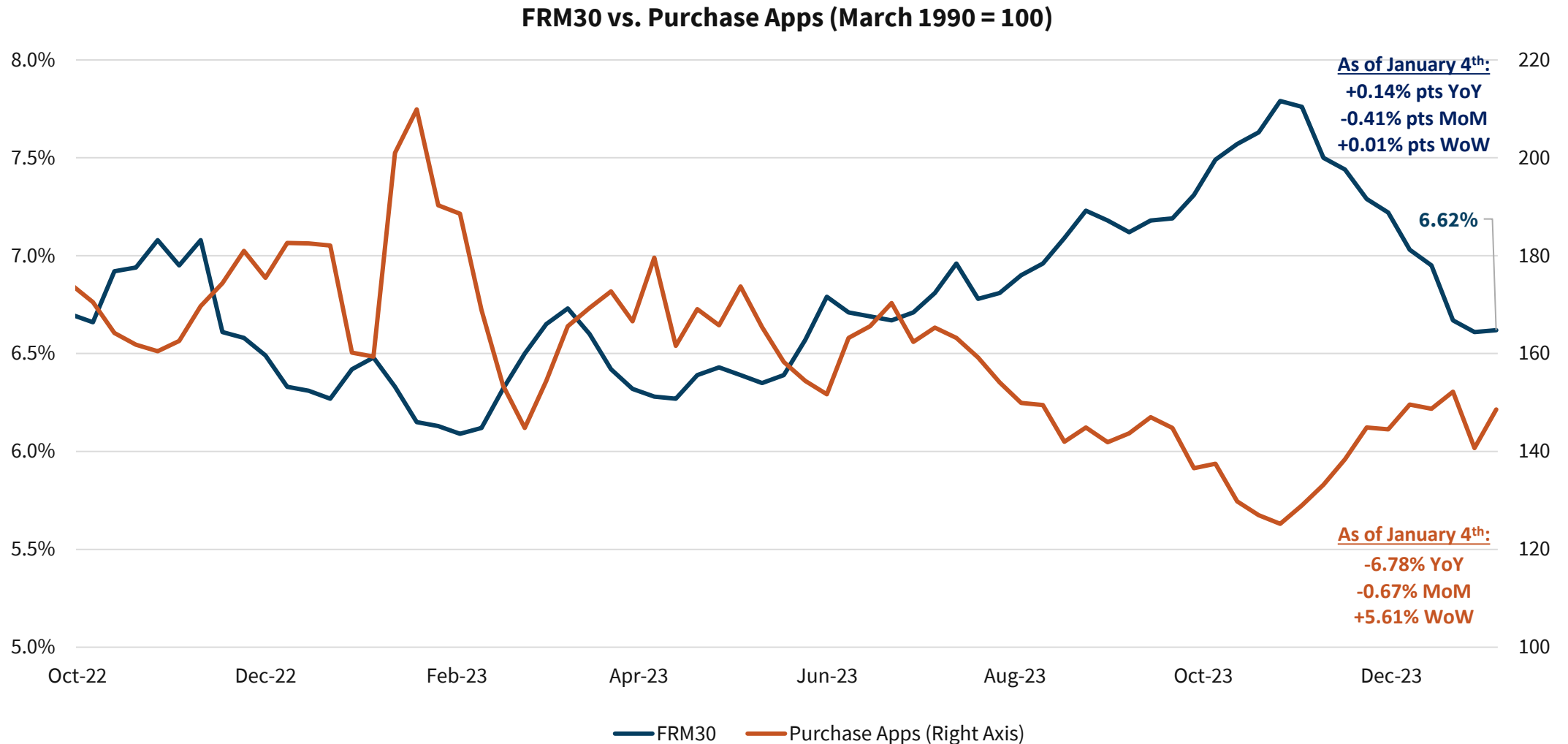
**Note: Inflation and existing home sales forecasts are based on the Fannie Mae Economic & Strategic Research August 2023 Forecast – Data in Forecast as of 8/10/2023. ESR does not produce a monthly nominal income forecast. This estimate is based on a nominal GDP approximation using the published CPI and real GDP forecasts.

***As of Fannie Mae Economic & Strategic Research October 2023 Forecast.



Purchase apps up from recent lows as rates drop to end 2023

Purchase activity remains lower year over year despite recent increase



Housing and mortgage market outlook

	2020	2021	2022	Forecast	
				2023	2024
Real GDP (SAAR, % Change)	-1.1%	5.4%	0.7%	2.6%	-0.3%
Unemployment Rate (%)	8.1%	5.4%	3.6%	3.6%	4.3%
Housing Starts (Percent Change Year-Over-Year)	1.380 million 6.9%	1.601 million 16.0%	1.553 million -3.0%	1.395 million -10.1%	1.277 million -8.5%
New Single-Family Home Sales (Percent Change Year-Over-Year)	822 thousand 20.4%	771 thousand -6.2%	641 thousand -16.9%	681 thousand 6.2%	673 thousand -1.2%
Total Existing Home Sales (Percent Change Year-Over-Year)	5.640 million 5.6%	6.120 million 8.5%	5.030 million -17.8%	4.104 million -18.4%	4.119 million 0.4%
Fannie Mae HPI (Annual Percent Change Q4/Q4)	10.4%	18.3%	8.0%	6.7%	2.8%
Purchase Mortgage Originations (Percent Change Year-Over-Year)	\$1,572 billion 18.5%	\$1,900 billion 20.9%	\$1,644 billion -13.5%	\$1,276 billion -22.4%	\$1,438 billion 12.6%
Refinance Mortgage Originations (Percent Change Year-Over-Year)	\$2,802 billion 146.7%	\$2,670 billion -4.7%	\$730 billion -72.7%	\$252 billion -65.5%	\$451 billion 79.3%
Refinance Share (%)	64%	58%	31%	16%	24%
30-Year Fixed-Rate Mortgage (Annual Average)	3.1%	3.0%	5.3%	6.8%	6.7%
10-Year Treasury (Annual Average)	0.9%	1.4%	3.0%	4.0%	4.3%



Resources for Economic and Housing Data

Contact Information:

- Hamilton_Fout@fanniemae.com

Recent Research:

- **“Lock in Effect” Not the Only Reason for Housing Supply Woes**
<https://www.fanniemae.com/research-and-insights/perspectives/lock-effect-not-only-reason-housing-supply-woes>
- **Workplace Flexibility May Help Address Affordability Concerns**
<https://www.fanniemae.com/research-and-insights/perspectives/workplace-flexibility-may-help-address-affordability-concerns>

General Links:

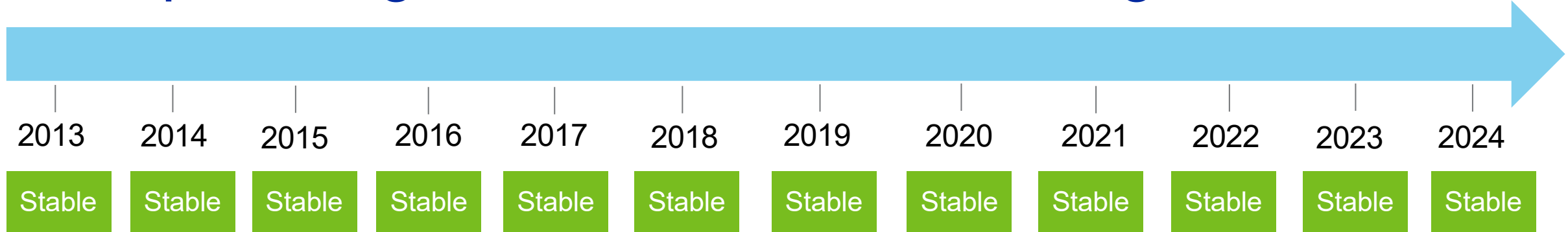
- **Economic & Strategic Research (ESR)**
<https://www.fanniemae.com/research-and-insights>
- **Mortgage Lender Sentiment Survey® (MLSS)**
<https://www.fanniemae.com/research-and-insights/surveys/mortgage-lender-sentiment-survey>
- **Home Purchase Sentiment Index® (HPSI)**
<https://www.fanniemae.com/research-and-insights/surveys-indices/national-housing-survey>
- **Fannie Mae Home Price Index (HPI)**
<https://www.fanniemae.com/research-and-insights/surveys-indices/fannie-mae-home-price-index>
- **Refinance Application-Level Index® (RALI)**
<https://www.fanniemae.com/research-and-insights/surveys-indices/refinance-application-level-index>





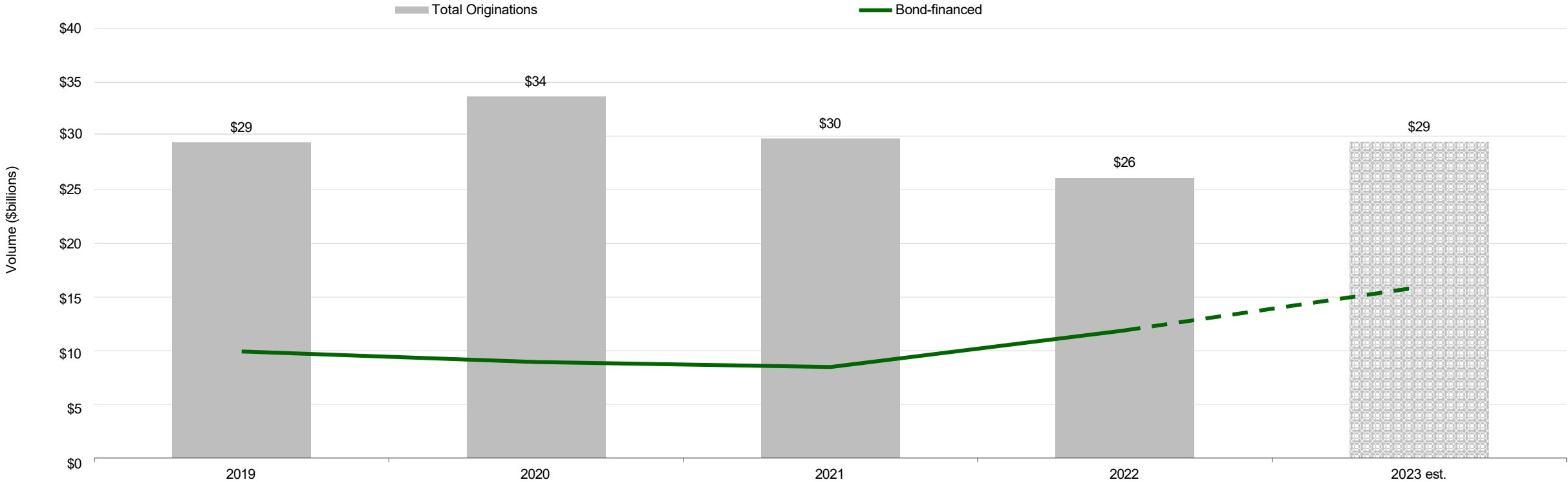
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2024 HFA outlook stable with higher-for-longer interest rates providing both benefits and challenges



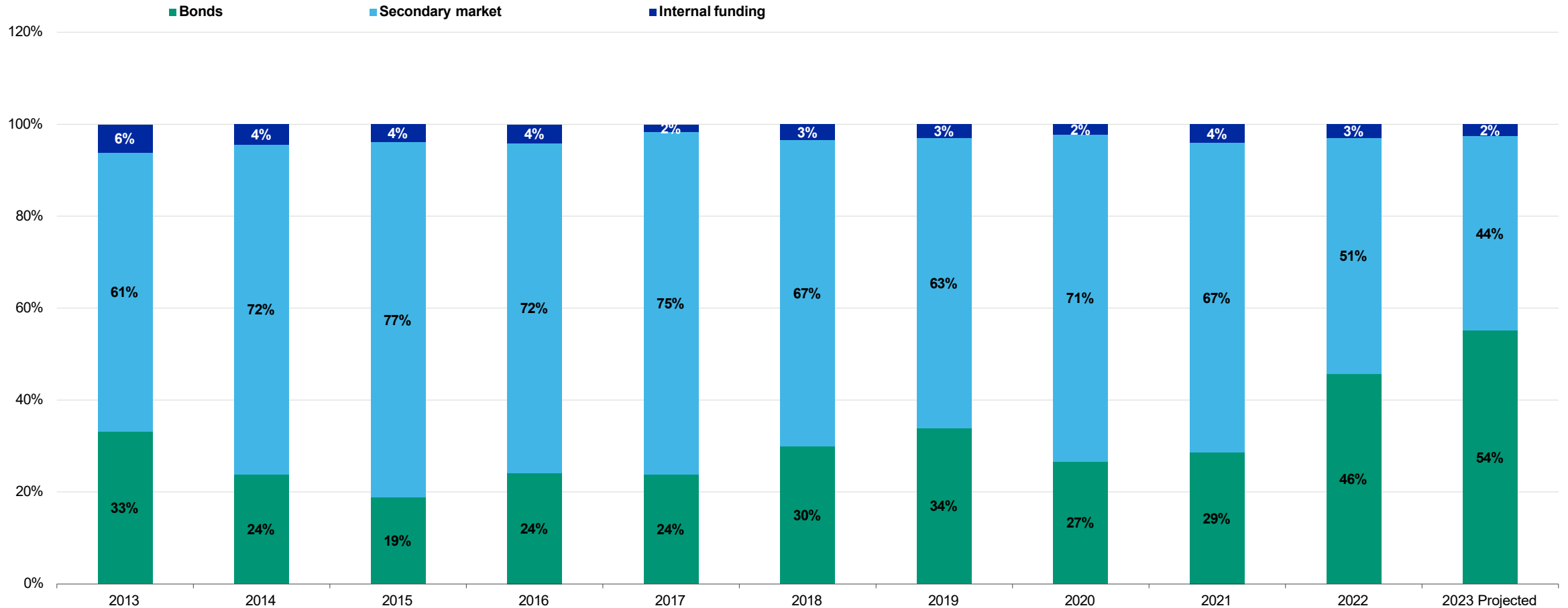
- » HFA's strong competitive profile supports solid single family loan originations
- » Higher-for-longer interest rates will drive steady HFA margins
- » The negative outlook on the US government presents a potential challenge, but strong financial and loan performance are mitigants
- » Multifamily portfolios will remain healthy due to demand for affordable housing

Bond-funded loan originations continue to climb, strengthening HFA balance sheets



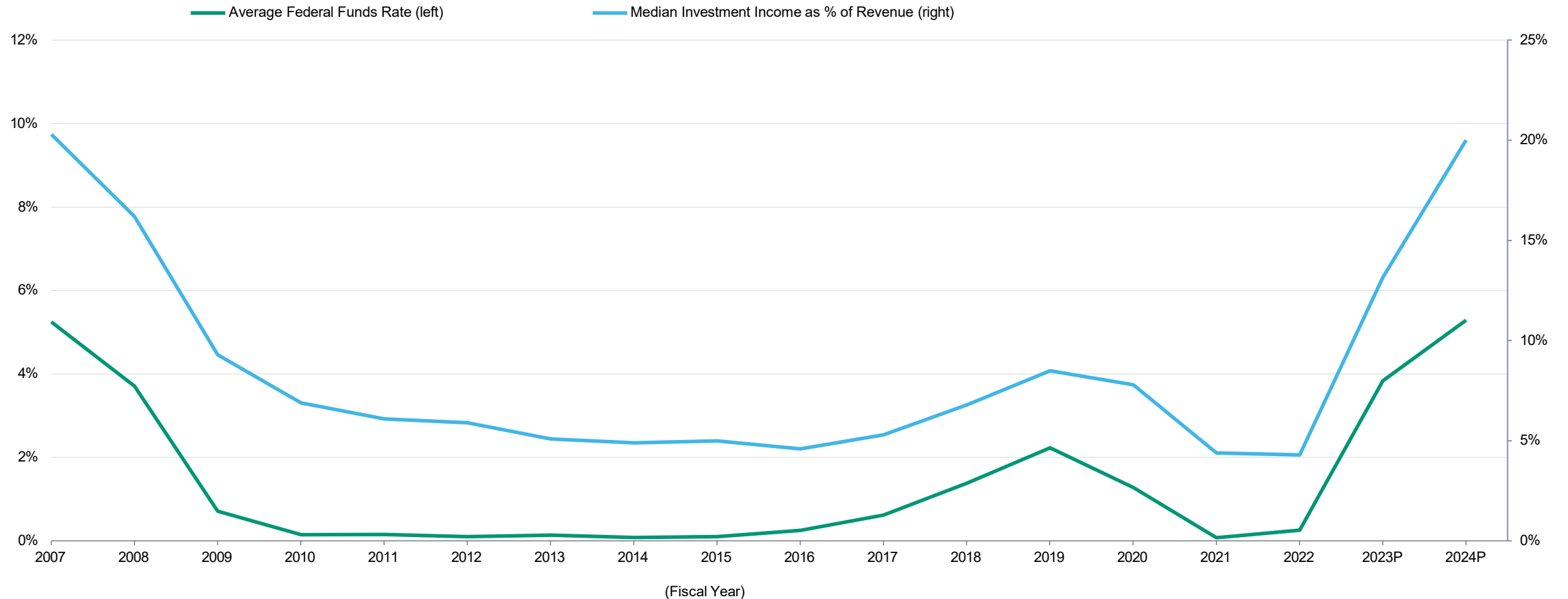
Source: HFA Surveys

Shift to bond funded originations continue to grow



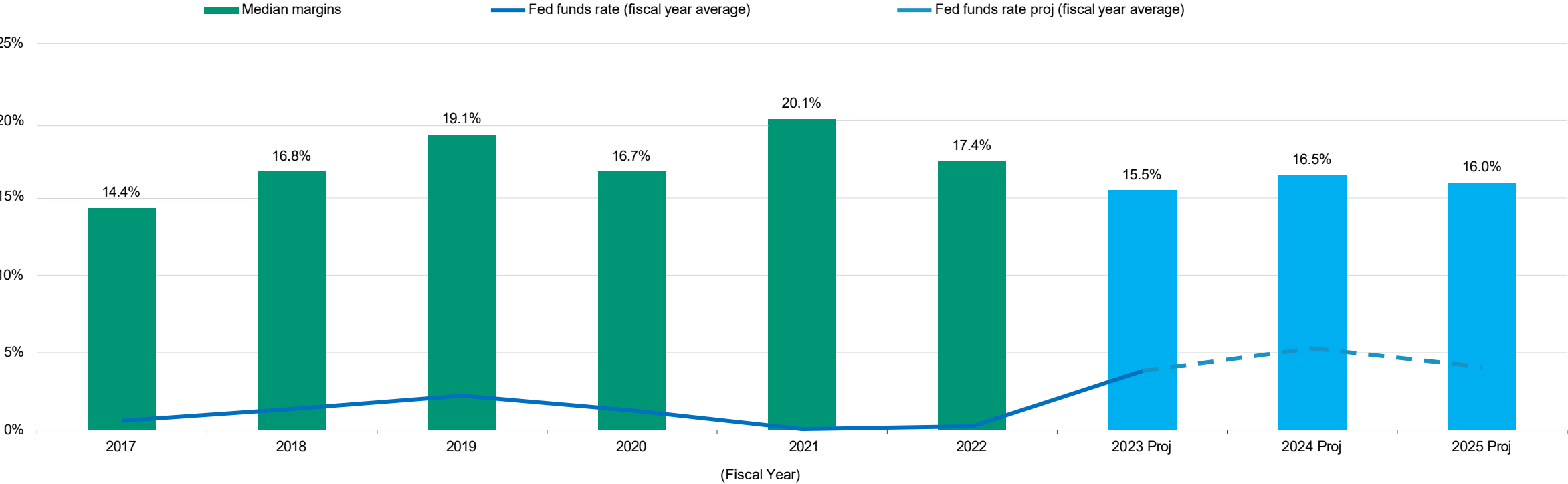
Source: HFA Surveys

HFA investment income will remain high in 2024



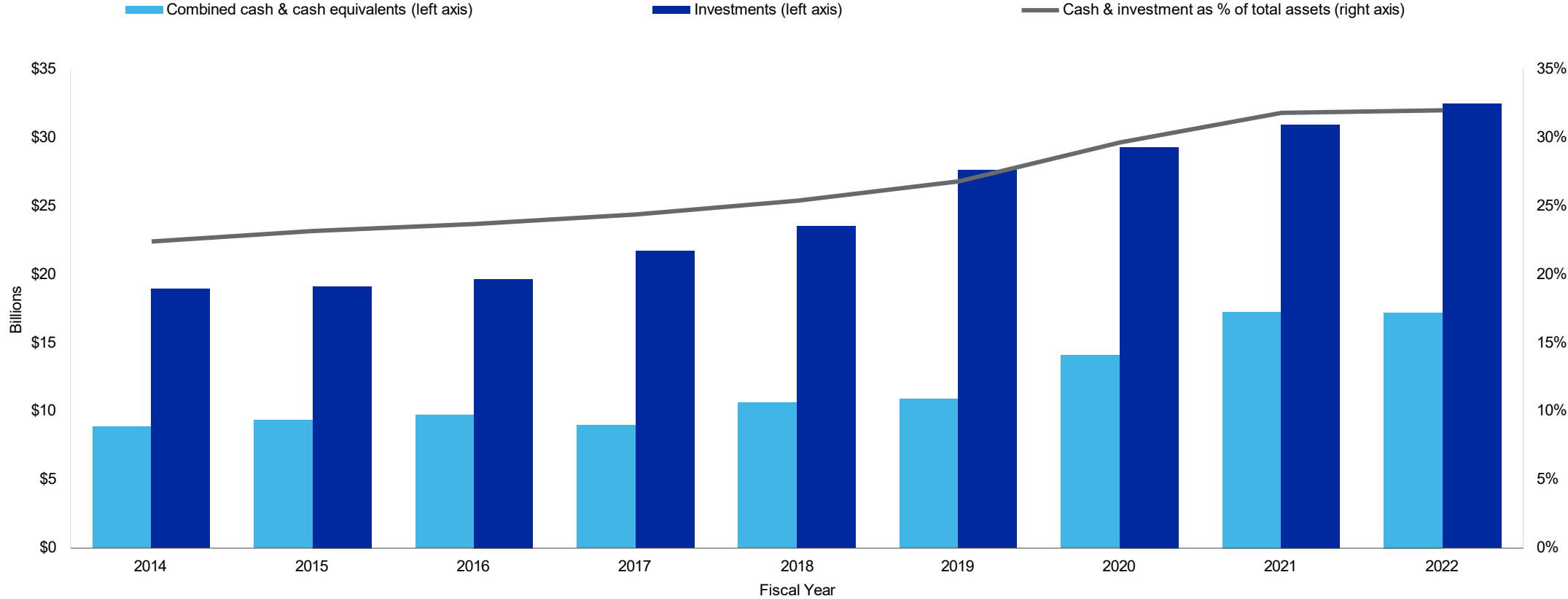
Sources: Moody's-adjusted HFA audited financial statements, Federal Reserve, Moody's Macroeconomic Board

HFA margins will benefit in from higher investment earnings and interest income



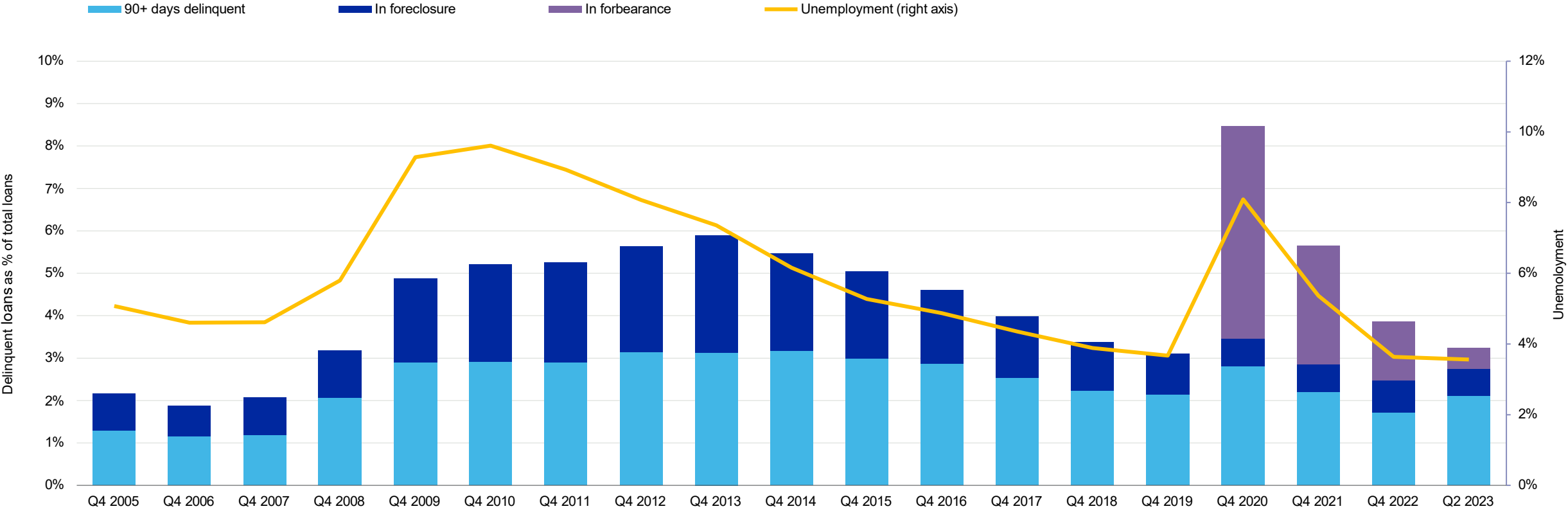
Sources: Moody's-adjusted HFA audited financial statements, Federal Reserve, Moody's Macroeconomic Board

Increasing share of cash and investments and high short-term rates will boost earnings



Source: Moody's-adjusted HFA audited financial statements

Loan performance favorably impacted by economic recovery and forbearance expiration

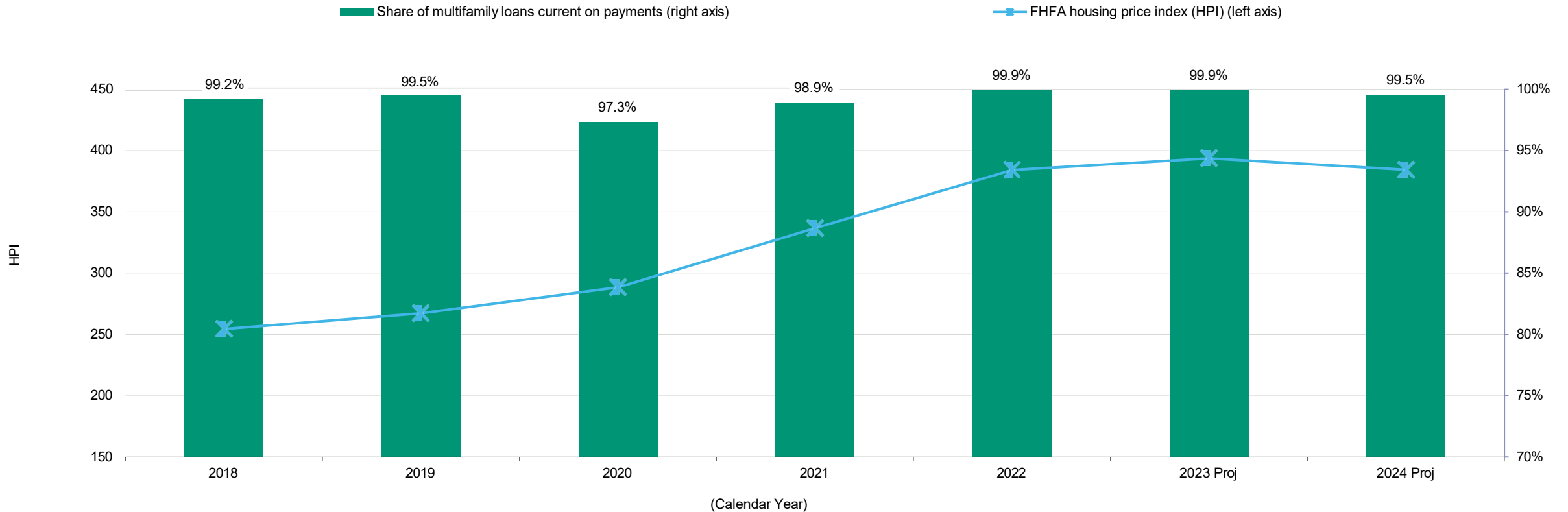


Sources: HFA Surveys; Moody's Macroeconomic Board

Despite federal support, most HFAs are resilient to US outlook revision

- » **HFAs are exposed to the federal government through counterparty risk**
 - HFAs are exposed to the federal government through mortgage insurance or securitization (MBS)
- » **Most HFA programs are resilient to downgrade of U.S. Government**
 - High overcollateralization levels offset stress case loan loss scenarios
 - Counterparty risk is assessed case by case as part of the methodology
 - Stand-alone programs 100% securitized of government insured move in lockstep
- » **Minimal number of program outlooks revised to negative**
 - Impacted credits were 100% MBS with very low asset-to-debt ratios
 - Conduits have no outlook and were not impacted but would move in lockstep with rating change

Rising home prices support multifamily portfolio strength



Sources: Federal Housing Finance Agency (FHFA), Moody's Macroeconomic Board

Strategic choices position State Housing Finance Agencies (HFAs) to weather future market downturns

Since the financial crisis in 2008, HFAs have increased loan enhancements, reduced variable rate debt, and begun secondary market financing to better equip them to withstand adverse macroeconomic and housing trends

How HFAs work

Financing sources

Bond issuance | Sale of loans on secondary market

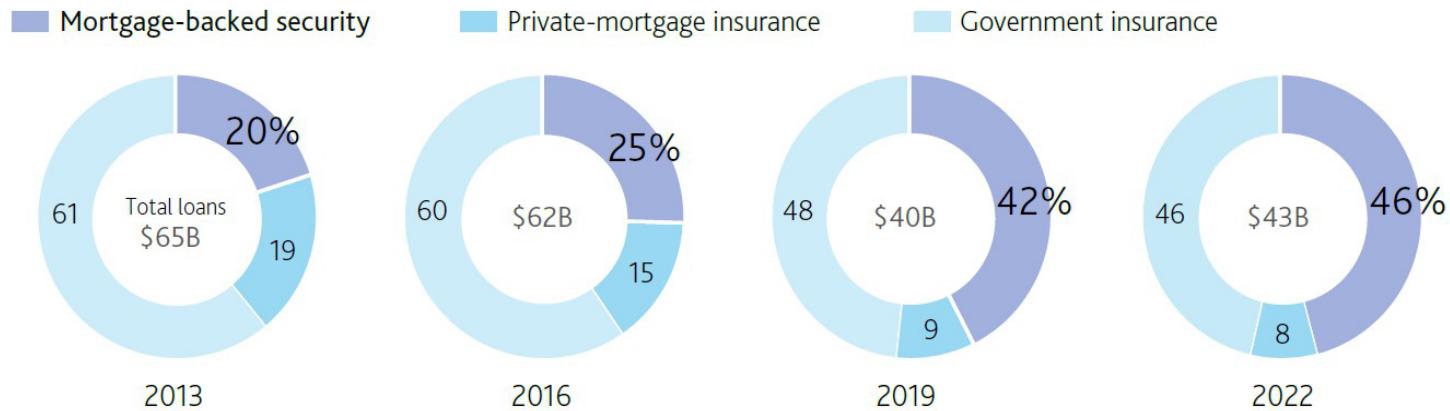


Loan

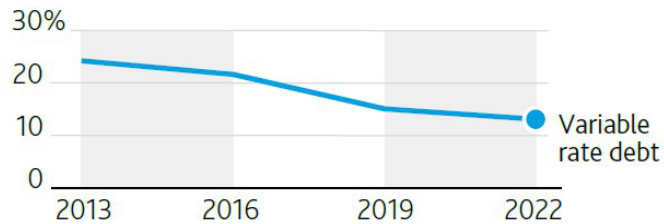


Loans for affordable homeownership and rental housing

HFAs have reduced balance sheet risk by increasing the proportion of mortgage-backed securities (MBS) in their portfolios



Debt structures have become more conservative as variable rate debt has declined

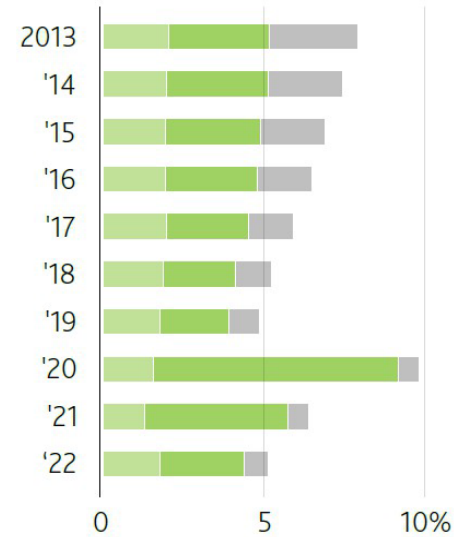


Multiple loan financing channels help HFAs respond nimbly to different market conditions



HFAs' decision to add more MBS will aid them as delinquency rates shift over time

60-89 days } Delinquent or in forbearance
 90+ days }
 In foreclosure



*Note:
 1) Periods prior to 12/31/20 do not have any loans in forbearance.
 2) For HFAs that did not include loans in forbearance in their 60-90 day or 90+ delinquency rates, we have added forbearance into the 90+ day category.

Source: Moody's HFA Survey



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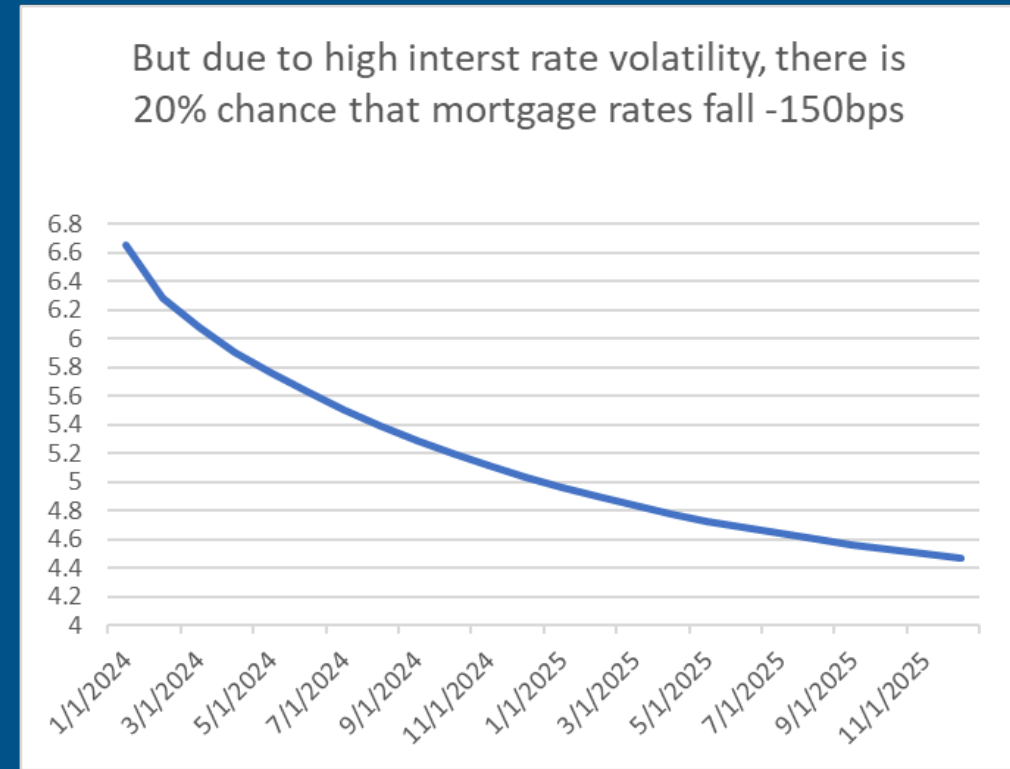
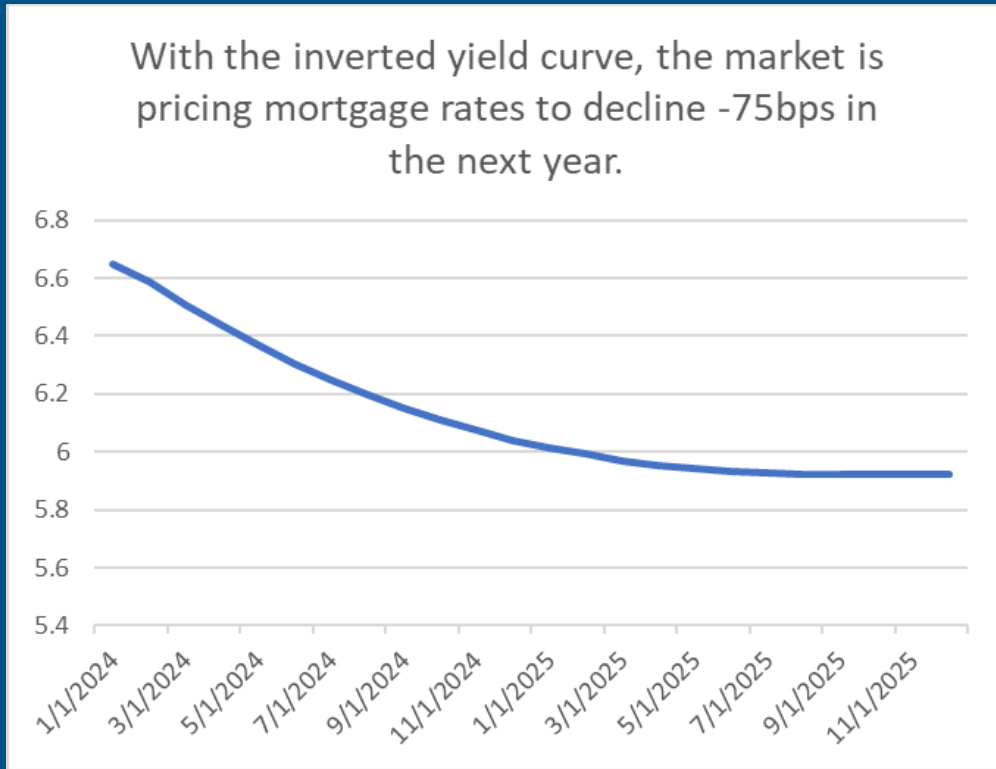


2023 in Review- TBA Pricing

- In efforts to curb inflation, the Fed continued its rate hiking path from 2022 into 2023, raising the Fed Funds rate to the highest level in 15 years.
- Mortgage yields were at a wide spread over Treasuries as a result of extreme interest rate volatility.
- As the yield curve inverted, the markets expectation that interest rates would fall in the future dampened premium pricing in the TBA market.
- As such, many HFAs found it difficult to post a full suite of Down Payment Assistance options on a daily basis; particularly those solely dependent on premium pricing via the TBA market.
- Baring the ability to post a full suite of DPA options, borrower eligibility at higher interest rates was negatively impacted.
- Muted specified pool demand further pressured HFA programs, particularly those with low volume and a lack of “specified stories”.



2023 in Review- MSR Values



Footnote: Forward mortgage rate derived from forward swap rate (source: Bloomberg). Partial durations of current coupon mortgage (source: Yieldbook)

- The current interest rate environment pressures MSR pricing lower (models are expecting newly produced loans to refinance within 1-2 years).
- After the FED cuts interest rates, the yield curve will steepen and implied volatility should decline. Interest rates will no longer be expected to decline into the future, resulting in an increase in MSR pricing on newly produced loans.
- Additionally, an improvement in the outlook for home prices will help the valuation of high LTV MSR.



2024 Outlook- TBA and Specified Pools

- A noticeable improvement in TBA execution should occur, provided there is a reduction in volatility, the Fed lowers the Fed funds rate and the yield curve steepens.
- As interest rates fall, call protection becomes increasingly more important and investors will seek bonds with significant call protection.
- HFA bonds offer significant call protection as they are backed by loans with repayable/forgivable and non-resubordinatable 2nd liens
 - Determining the structure of the 2nd lien and defining an appropriate resubordination policy is of upmost importance in the current environment as this impacts the premium investors are willing to pay for HFA bonds.
- Premium pricing improvement by way of the TBA market is largely dependent upon the Fed's actions in 2024.
- Projections are calling for 150+ bps in rate cuts. Should that occur, mortgage rates will decline significantly. However, if the rate cuts are less material, i.e. 50 bps, current coupon yields could be potentially unchanged resulting in little improvement in TBA premium.



2024 Outlook- MSR Values

- MSR values are largely dependent upon modeled values of Volatility, Home Price Appreciation/Depreciation, Default Risk, Prepayments Speeds and Borrower Profile.
- Negative for MSR Values:
 - Fast prepayment Speeds- If rates are expected to decrease, borrowers are expected to prepay, lowering MSR values.
 - Default Risk- In an HPD environment, default risk increases.
 - Weak credit profile- Low FICO, High LTV, High DTI, small loan balances
- Positive for MSR Values:
 - Slow prepayment speeds- If rates are expected to increase, prepayments are expected to be muted, raising MSR values.
 - Default Risk- In an HPA environment, default risk decreases.
 - Robust credit profile- High FICO, Low DTI, large loan balances
- As rates are expected to decline in 2024, prepayments are also expected to increase, albeit muted for HFA loans due down payment assistance offered via repayable 2nd liens. Home Price Appreciation is also projected to be positive in 2024, resulting in lower expected default rates. Both of which are positive for MSR values!



2024: Forecast and Pricing Impacts

- All eyes will be on the Fed as the market looks for direction by way of frequency and amount of rate cuts, resulting in lower rates and a return of premium pricing.
- A keen focus on all components of HFAs programs should be front and center as to offer a program that is mutually beneficial to both borrowers and investors; ultimately offering the best product and lowest rates to borrowers.
- Areas of Focus:
 - Structure of 2nd lien- Impacts Specified Payups and MSR Values
 - Resubordination Policy- Impacts premium investors are willing to pay for HFA bonds and MSR values
 - Credit Profile of borrowers- Impacts MSR Values
 - MSR Values- Driven by borrower profile and performance as well macro-economic environment



HOUSING AND BOND MARKET
UPDATES FOR THE NEW YEAR

2024 NCSHA INSTITUTE
TBA MARKETS

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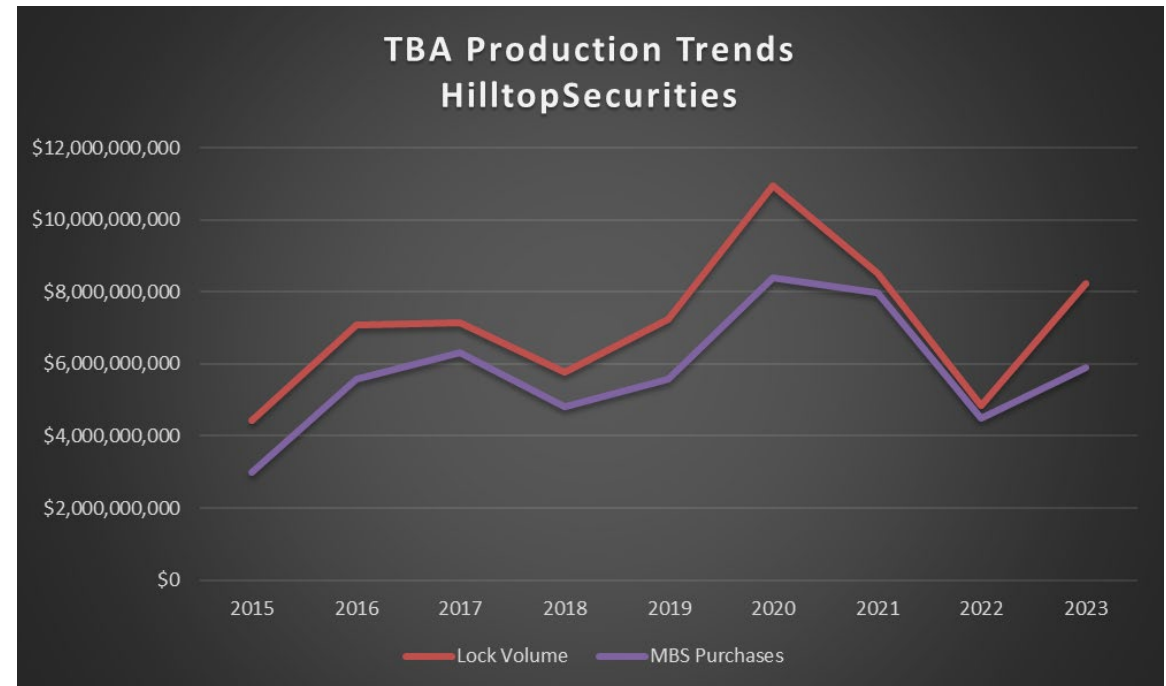
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TBA Market Update – A Strong Late Year Comeback

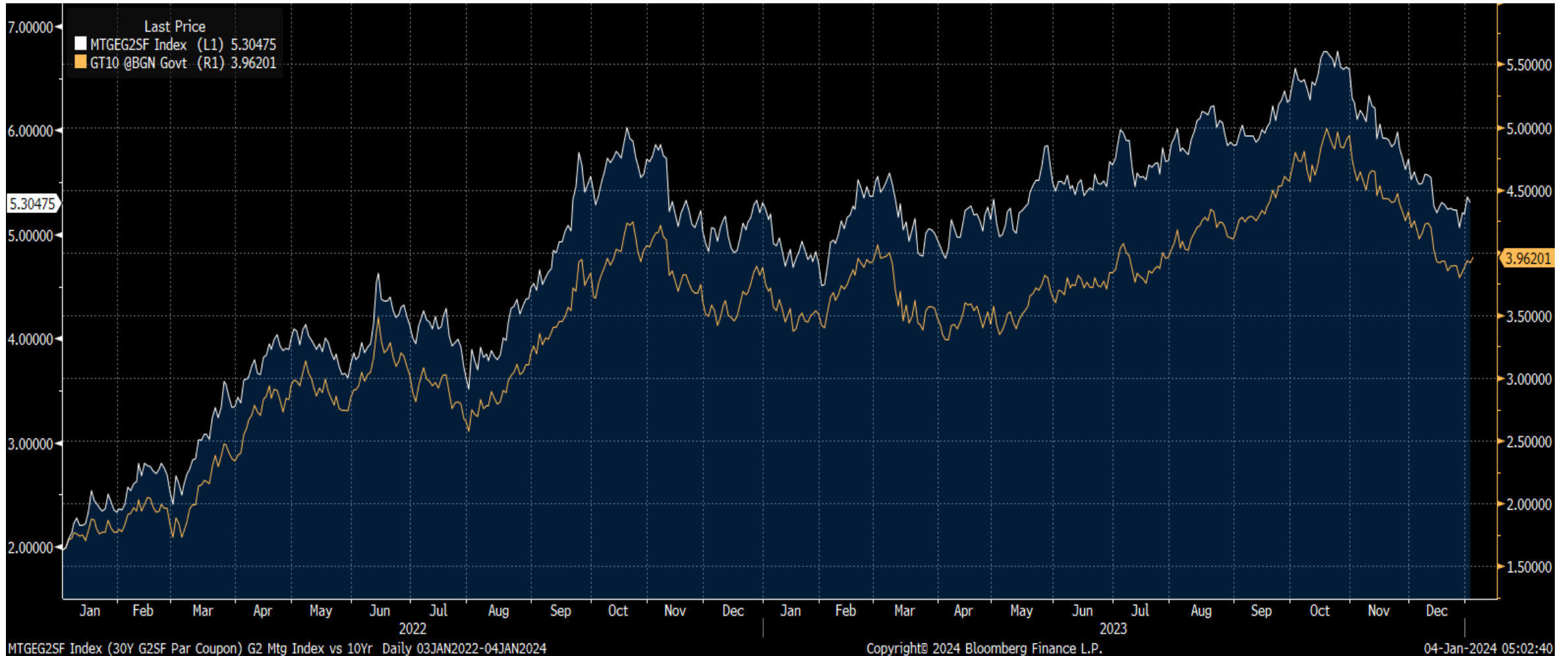
- Despite unprecedented volatility and multi-decade high in mortgage rates, TBA's mounted a strong comeback in November and December
- Driven primarily by Fed “Dovish” tone and Investor “Disinflation” conviction
- The “Prepay Protection” trade has also seen a strong rally driven by both the street and end investors
- Areas of market that haven't healed completely:
 - Demand from Banks and CMO buyers
 - Overseas buying given the strong dollar

Production Trends

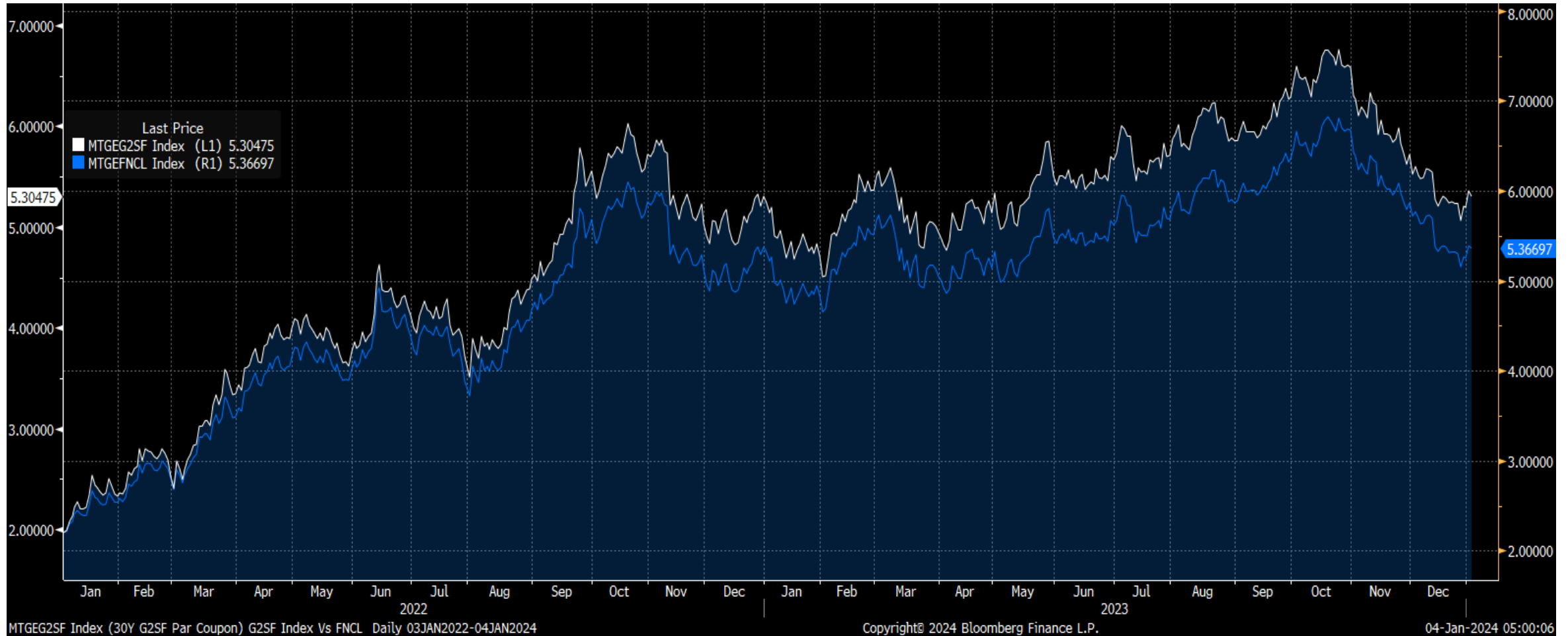
- HFAs continue to see robust TBA volume despite record MRB issuance
- 2023 was another very strong year in lock volume for HTS HFAs
 - 2023 locks of \$8.6 billion compared with \$4.8 billion in 2022 – up almost 80%
- Since July 2012 represented 18 state programs and over \$70 billion in locks with \$54 billion in MBS purchases
- 11 out of 18 HTS HFA partners using both MRB and TBA to fund single family activity



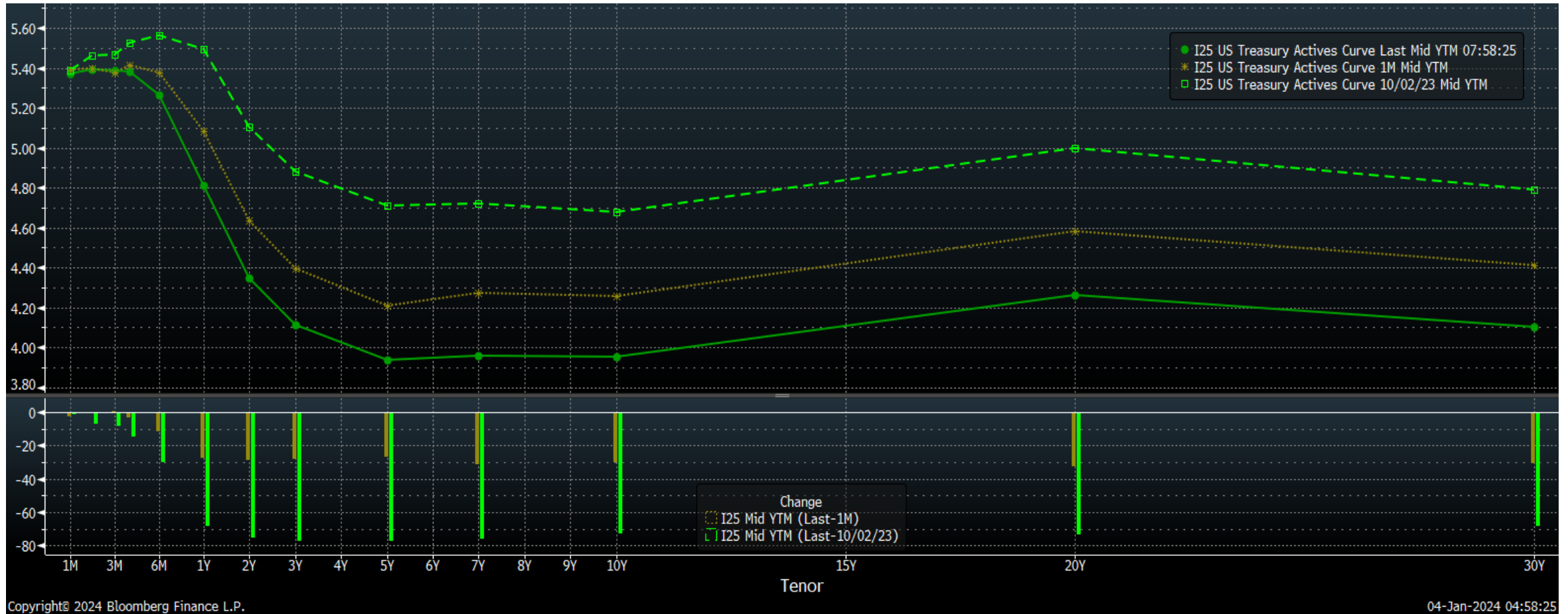
Ginnie Mae II Current Coupon & 10yr Treasury yield



Ginnie Mae II Current Coupon & Fannie Mae Current Coupon



Treasury yield curve (current, 1 month ago and 10/1/23)



Market Dynamics Haven't Changed Much

- Lack of supply – exacerbated by slow prepayments and high mortgage rates
- Record home prices
- Strong demand for housing due to 2–4 million-unit shortage
- Institutional investors owning rental housing not selling

Other Factors

- Ailing mortgage industry, shrinking profits (6 consecutive losing quarters according to MBA)
- Despite recent rally, premium in higher coupon TBA hasn't recovered
- Volatility is here to stay as evidenced by recent selloff

Lack of Premium in Higher Coupon TBA

TBA		1) Actions		3) Settings		Fixed Income Trading			
22:21		Outright		Switch		Bfly			
* Market Closed *									
4) MBS		5) Swaps		6) Basis		7) Butterflies			
8) TBA30		9) TBA15							
21) UM30		22) UM15		23) GD30		24) GD15			
25) GN30		26) GN15		27) GNII					
5.0		5.5		6.0					
Jan	98-20 / 25+	- 12	100-02+ / 09+	- 08	101-06 / 13	- 06+			
Feb	98-21+ / 27	- 12	100-03 / 10	- 07+	101-04+ / 11+	- 07			
Mar	98-23 / 26+	- 12	100-04 / 08	- 07+	101-03+ / 08+	- 06+			
Jan/Feb	- 01+ / - 01 ¹ / ₈	--	- 00 ⁵ / ₈ / - 00 ¹ / ₄	+ 00 ¹ / ₈	01 ³ / ₈ / 01 ³ / ₄	+ 00 ¹ / ₄			
Feb/Mar	- 01 / - 00+	- 00 ¹ / ₈	00 ¹ / ₄ / 00 ³ / ₄	--	01 ⁵ / ₈ / 02	- 00+			
Jan/Mar	- 03 / - 01	--	- 01+ / 01+	--	02+ / 04+	--			
6.5		7.0		7.5					
Jan	102-04 / 10+	- 02+	102-21 / 30+	- 02	102-14+ / 13	--			
Feb	101-31+ / 06+	- 03	102-17+ / 27	- 02	/	--			
Mar	101-27+ / 02+	- 03	102-08+ / 22	- 05	/	--			
Jan/Feb	03 ⁷ / ₈ / 04 ¹ / ₄	+ 00+	03 ¹ / ₈ / 03+	+ 00 ¹ / ₈	/	--			
Feb/Mar	03 ⁵ / ₈ / 04	- 00 ¹ / ₈	02 ⁵ / ₈ / 10 ³ / ₄	--	/	--			
Jan/Mar	/	--	/	--	/	--			
Benchmarks				Roll Analysis-G2SF			Jan/Feb		
Treas 2Y	99-23+ / 23 ³ / ₄	4.391 / 387	- 03 ³ / ₈	Cpn	Cpr	Drp	B/E Drp	B/E Rt	B/E Cpr
Treas 3Y	100-19 / 19 ¹ / ₄	4.158 / 155	- 06 ¹ / ₄	5.00	2.06	-1.500	-1.20	5.51	0.00
Treas 5Y	98-30 ³ / ₄ / 31	3.982 / 980	- 11	5.50	2.48	-0.500	-0.30	5.47	20.03
Treas 7Y	98-15 / 15+	4.003 / 001	- 15	6.00	2.36	1.500	0.69	5.08	0.00
Treas 10Y	104-01 / 01+	4.001 / 999	- 22	6.50	2.84	4.500	1.69	4.33	0.00
Treas 30Y	110-04+ / 06	4.154 / 151	-1-14+	7.00	2.75	3.500	2.81	5.13	0.00

For detailed roll analysis, please right-click a cell with a price, and select "RA"

TBA mortgages – what will it take to see meaningful recovery?

- A steeper yield curve
- More buyers
 - Banks need to get past regulatory overhauls, healing balance sheets
 - USD needs to weaken so overseas has more buying power
- The need for clarity on Fed's roadmap for sidelined investors to come back
- Range bound treasury yields, which should in turn translate to lower volatility
- More housing supply – unlikely to happen overnight