Peter DiMartino
(212) 783-7871
pdimartino@sbi.com

Nonagency CMO Issuance: A Tale of Two Markets

We have been suggesting that nonagency investors look away from traditional new-issue nonagencies due to the sector's technical richness. Instead, we recommend that investors examine opportunities in nontraditional sources of mortgage collateral. Nonagency issuance is a tale of two markets because as traditional nonagency issuance has evaporated, issuance of nontraditional MBS and HEL ABS has skyrocketed collectively. As a result, investors are discovering several "off-the-run" issuers, each with their own unique blend of collateral characteristics. Although nontraditional MBS and a significant percentage of HEL ABS are backed by first-lien mortgage collateral, investors should become familiar with the variety of borrower profiles found in many of these "off-the-run" names. In this article, we examine issuance trends, and compare selected collateral characteristics for issuers in each mortgage subsector.

The top ten MBS issuers account for 97% of nonagency volume in 1996.

Traditional nonagency supply in 1996 (defined here as "A" credit quality borrowers with maximum debt-to-income ratios in the mid-30% range) arrived mostly in the first half of the year, totaling about $16 billion. In the four months since, investors saw just $5 billion in traditional nonagencies. Figure 3 ranks the top ten issuers in MBS and ABS. As shown, RFC, GE, and NASCOR/Pru Home dominate MBS issuance, and account for two-thirds of the volume. The remaining $6 billion of nonagency MBS came from non-traditional sources of collateral. As shown in Figure 3, Indy MAC's RAST program issued almost half that amount, and RFC issued another $1.3 billion on their RALI shelf. RAST and RALI are known for their "stated-income" and "no-ratio" documentation categories, as well as a prevalence of investor properties and conforming balance loans. Long Beach Mortgage, and Option One Mortgage ("B&C" issuers whose collateral is found in Salomon Brothers, AMRESCO, and ContiMortgage shelf registrations), shown in Figure 1 as well, issued another $2 billion collectively. In all, the top ten MBS issuers account for 97% of the issuance in nonagency MBS. Furthermore, 25% of the total nonagency MBS volume was issued with non-traditional sources of collateral.

Figure 3. Top-Ten Mortgage-Related Issuers by Market, Dollars in Billions, Oct 96

	MBS			ABS		
Rank	Issuer	Volume	Percentage Market Share	Issuer	Volume	Percentage Market Share
1	RFC	$9.0	33%	The Money Store	$2.5	11%
2	GE	4.8	18	ContiMortgage	1.9	8
3	NASCOR/Pru Home	4.2	15	United Companies Financial Corp.	1.6	7
4	Indy MAC/RAST	2.7	10	Merrill Lynch	1.3	6
5	Salomon Brothers	1.4	5	RASC and RFMSII	1.2	5
6	RFC/RALI	1.3	5	Beneficial Corp.	1.2	5
7	DLJ MAC	1.0	4	EquiCredit	1.1	5
8	Bear Stearns	0.8	3	Advanta	1.0	4
9	Countrywide	0.7	2	Aames	1.0	4
10	Structured Asset Securities Corp.	0.6	2	IMC	0.9	4
Total Market Volume		$27.0			$23.6	
Total Issuers		22			42	
Top Ten Issuers Market Share		97%			59%	

Sources: Inside Mortgage Securities and Salomon Brothers Inc.

HEL ABS volume more than doubled since 1995, and when combined with nontraditional MBS, represent 140% of traditional nonagencies issued in 1996.

Another source of nontraditional mortgage collateral is found in the HEL ABS market. Again, backed primarily by first-lien mortgage loans, this sector is chiefly comprised of "B&C" mortgage collateral. HEL ABS issuance has more than doubled since 1995, topping $23 billion, and represents about 20% of the entire ABS market. In total, issuance in nontraditional MBS, together with HEL ABS represents about 140% of traditional nonagencies issued in 1996. Market share in HEL ABS, however, can be characterized as "fragmented" in relation to that of traditional nonagencies. As shown in Figure 3, 42 issuers are responsible for the total volume in 1996. Furthermore, the top ten HEL ABS issuers hold just 59% market share. Many of the remaining issuers (not shown in

Figure 3) have made their debuts in 1996. Most of the top ten issuers have improved their information flow, and support their transactions in the secondary market. We have compared the collateral characteristics of some of the larger, and more well known issuers in the HEL ABS market with those of other nontraditional issuers in the nonagency mortgage market.

Figure 4. Comparison of Nontraditional Sources of Collateral

Selected Issuers[a]	Market	Credit Sector[b]	Fixed-Rate Percentage	First Lien	Max Debt Ratio[c]	Max LTV Ratio[d]	Avg. Loan Balance
INDY MAC/RAST	MBS	"A-"	100%	100%	38%	95%	$140
RALI (RFC)	MBS	"A-"	80	100	40	95[e]	110
Long Beach	MBS	"B&C"	40%	100%	55%	90%	$100
Option One	MBS	"B&C"	20	100	60	90	100
Advanta	ABS	"B&C"	47%	90%	55%	100%[f]	$60
ContiMortgage	ABS	"B&C"	77	90	55	95[f]	60
EquiCredit	ABS	"B&C"	96	80	50	100f	50
RASC (RFC)[g]	ABS	"B&C"	32	100	60	95[f]	125
The Money Store	ABS	"B&C"	71	80	NA	90[f]	60
United Companies Financial Corp.	ABS	"B&C"	50	90	45	100[f]	60

[a] INMC and RAST are securitized under CWMBS shelf. RALI and RASC are part of RFC and have their own shelf registration. [b] Issuers have similar but different credit grades. [c] Where applicable (does not apply to no income/no ratio programs), refers to total expense ratio. [d] Highest LTV permitted in the pool. [e] Excludes "Merrill 100" loans. [f] Combines first & second lien mortgages (CLTV). [g] RASC is permitted to securitize seconds, but have not to date.
Sources: Indy Mac, RFC, Long Beach, Option One, Advanta, ContiMortgage, EquiCredit, The Money Store, United Companies Financial Corp., Prospectus, Bloomberg, Moody's, Fitch and Salomon Brothers Inc.

Some important differences, as well as similarities, exist among the selected issuers in Figure 4. Some observations follow:

• At present, MBS issuers securitize only first-lien mortgages; HEL ABS usually include second-lien mortgages in their securitization programs;

• "B&C" issuers in either market allow debt-to-income ratios ranging from 40-60%; "A-" credits peak at 40% debt-to-income (applies to those programs that require income verification);

• Maximum LTV ratios range from 90-95% in the MBS market for the issuers we surveyed; due to second-lien mortgages, maximum combined LTV ratios can reach 100% in the ABS market, although first mortgage LTVs generally range from 80-90%;

• For "A-" credit borrowers, full documentation underwriting (not shown) is less prevalent (due, in part, to self-employed borrowers with larger down payments) than for "B&C" borrowers, where credit concerns dictate the level of documentation;

• Almost all of the mortgage collateral backing "B&C" transactions are owner-occupied properties (not shown), while "A-" programs have a greater percentage of investor properties;

• Loan balances in "A-" and "B&C" MBS programs average $100,000 or greater, and average $50,000-$60,000 in HEL ABS (please note that we show the average loan balance, however in HEL ABS, ARM loans tend to have much higher loan balances than fixed-rate loans);

• Most HEL ABS use bond insurance to provide credit enhancement; some "B&C" MBS transactions recently have been issued using subordination as credit enhancement, thus providing another avenue for investors to take credit risk.