



# MIAC Perspectives

Spring 2007

## SFAS 157:

### It's Big Stuff for Mortgage Bankers

In September 2006, FASB accepted a sweeping new standard redefining a core accounting concept – Fair Value. This new standard supplants over 60 prior FASB pronouncements. Because the scope of the changes is so pervasive, FASB gave firms until November 2007 to adopt the new standard. Mortgage companies are required to carefully review and update their asset valuation methodologies for their MSR's, Whole Loans (both in the pipeline and portfolio), retained Residual Interests and all of their hedge instruments.

Not only must each firm re-evaluate their asset valuation methodologies but also the business control procedures that support these valuation methodologies. Each procedure must be reviewed and revised. Consequently, the SFAS 157 standard represents considerable challenges for implementation but also will have a significant impact on the mortgage industry.

In MIAC's last quarterly newsletter, Tina Reid, Senior Vice President and co-head of MIAC's Secondary Solutions Group, outlined the implications of SFAS 159 for mortgage bankers' pipelines. In this issue, Sa-

chit Kumar, Managing Director and Head of MIAC's Capital Markets Group, highlights some important issues for effectively implementing SFAS 157 for MSR's. In subsequent quarterly editions, MIAC will address some of the SFAS 157 implications for Whole Loans, Residual Interests and Interest Rate Derivative instruments.

The tasks ahead for mortgage industry participants in understanding the implications for SFAS 157 are two-fold. First, a mortgage company CFO must understand the very new definition of Fair Value identified in SFAS 157 – a daunting task given the creation of new terms and principles to a very core accounting concept. Secondly, and even more challenging, mortgage companies must sort through how to implement these new interpretations for each of the mortgage assets and liabilities. In this newsletter, we will first look at those new Fair Value concepts likely to be germane to MSR valuation. Then, we will undertake an analysis of SFAS 157 potential impact for implementing SFAS 157-compliant MSR valuation methods.

**Bob Husted**   **Paul Van Valkenburg**

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# SFAS 157: A Walk Down Implementation Lane



By Sachit Kumar  
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SFAS 157 will have a profound impact for all holders of MSR, not just those few firms who elected Fair Value reporting under SFAS 156. The Fair Value methodology is the standard disclosure for SFAS 140 Impairment Testing of MSR. Therefore, every holder of MSR must employ a newly defined Fair Value method for Impairment Testing of their MSR.

In addition to new procedures for Impairment Testing, mortgage companies will also need to alter their methods for initially booking MSR. SFAS 156 requires that MSR be booked at Fair Value and no longer at Relative Fair Value, which involves a cost accounting component. Both of these previously established Fair Value disclosures are likely to undergo significant adjustments once mortgage companies are compliant with the new definition of Fair Value under SFAS 157.

We'll briefly describe some of the new concepts in SFAS 157 and then present some of the implications for adapting your MSR valuation methodologies to be SFAS 157 compliant.

## Significant New Concepts of Fair Value in SFAS 157:

Exit Price

Market-Based vs. Entity-Specific Valuation

Fair Value Hierarchy

Principal (or Most Advantageous) Market

Highest and Best Use Analysis

Blocking Factor

Expanded Disclosure and Model Input Assumptions

## Exit Price:

The definition of Fair Value from SFAS 157 is "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

In addition, the historical standard fair value market conditions apply:

An orderly transaction

Arm's length transaction with disinterested parties involved

No transaction costs (Broker fees)

Includes transportation costs (Recording fees)

An important distinction that SFAS 157 makes is that the Exit Price is not the Entry Price or the cost to acquire the asset. The example one leading accounting firm uses is the market dynamics of purchasing a new car. The buyer pays \$50K for the new car, but as soon as he drives off the showroom floor, the now slightly new car could be sold for \$40K. The Exit Price of the slightly new car is now substantially discounted to reflect the reality of this market's dynamics. This Exit Price of \$40K is what the new Fair Value standard requires the users to disclose even though the cost of the new car was \$50K. This has tremendous implications for mortgage companies.

Under SFAS 156, MSR values must be initially booked at their Fair Value, regardless of whether the mortgage company has elected to adopt the Fair Value method for reporting MSR values on a go-forward basis or utilize the long-standing LOCOM (Lower of Cost or Market) disclosure. The initial MSR Fair Value must be the Exit Price. For many mortgage companies that have been complying with the Relative Fair Value methods for initially booking MSR values, this will cause some significant changes to both their accounting practices as well as their business practices.

Mortgage companies will need to:

- Regularly review Flow, AOT, SRPs, and Co-issue Servicing multiples.
- Maintain MSR valuation assumptions consistent with current market Bulk and Flow pricing.
- Understand the implications of the migration from Flow MSR to Bulk MSR pricing.
- Utilize a widely accepted software model that can demonstrably replicate MSR market prices.

### Bye, Bye MSR Impairment Cushion?

Does this mean that newly originated (off the show room new car) MSR values will be priced more consistently with Bulk (slightly older new car) MSR values in the future? If a mortgage company must test for impairment one calendar quarter after origination and interest rates and economic conditions haven't changed significantly, then the Fair Value derived from the impairment test needs to be very close to the amortized initial book basis in order to avoid challenging how the MSR asset was initially booked. This impairment test will, if done in a manner consistent with SFAS 157, be consistent with Bulk MSR valuations methods, assumptions, and market execution.

As a result, a currently common accounting practice — that of initially booking the MSR values at values significantly below Fair

Value and therefore creating a cushion against future impairment — will be jeopardized. MIAC believes that changing the initial booking of MSR values to Fair Value could have a dramatic effect on the mortgage banking industry.

One likely consequence of this change will be that a much larger number of mortgage companies will elect to hedge their impairment risk in their MSR values. Whether they set up distinct MSR hedging programs or utilize other mark-to-market balance sheet assets, they will surely need more effective risk management solutions.

### More MSR Hedging?

Another likely consequence is that more mortgage companies will migrate to the SFAS 156 Fair Value disclosure for their MSR values on an ongoing balance sheet basis. If the initial accounting cushion is removed and LOCOM restricts their ability to write up their Fair Value gains, then more mortgage companies will be motivated to adopt Fair Value disclosure of their MSR values. They won't want to hedge a LOCOM asset and not be able to write up their assets when the hedges decline in value.

Also, the market value declines in MSR values won't be disclosed as "impairments", a meaningful distinction for the readers of these financial statements. Moreover, without the burdens of FAS 133 effectiveness testing, setting up simple MSR hedging programs can be viable solutions for addressing their earnings volatility concerns.

### Market-Based vs. Entity-Specific Valuation:

For holders of publicly traded fixed-income securities, the Market-Based vs. Entity-Specific valuation will have no impact. However, for holders of MSR values, a frequent point of clarification in the current valuation practice is whether a particular valuation represents a market valuation or an "economic" valuation. A common practice in MSR valuations is for the holder of the MSR values to value the assets' "economic" value or the Entity-Specific valuation. An economic valuation generally means an

Continued from Page 3

entity-specific, or to some degree entity-specific, valuation where input pricing assumptions are derived from the company's own experience with the MSR asset.

The particular parameters or input assumptions that are often made entity-specific are:

- o T&I Multipliers
  - o Marginal Costs to Service various loan products
  - o Escrow Earnings Rates
  - o Geographic adjustments to prepayments or delq/FCL behavior
  - o Prepayment behavior
  - o Delq/FCL behavior
  - o Entity-Specific OASs
- Entity-Specific Aggregation Levels

Inconsistencies in any of these input assumptions with market consensus assumptions will result in MSR valuations differing from a market price. Clearly, an independent third-party MSR valuation or an appropriate comparison to benchmark Generic Servicing Assets (GSAs™) pricing will provide an important independent verification of the input pricing assumptions.

Fair Value Hierarchy:

One of the most important components of the new SFAS 157 standard is the new hierarchy associated with the disclosure. If a Fair Value was derived from a market source with a higher level of reliability, then this reliability level is now included in the financial statement. Fair Values will be categorized as Level 1, 2 or 3 Fair Values.

Here is a brief summary of the definitions of the fair value levels.

*Level 1:*

- Market Observable: Quoted Price

*Level 2:*

Observable market data other than Level 1 inputs

- Quoted prices for similar assets or liabilities in active markets

- Quoted prices for identical or similar assets or liabilities in inactive markets

- Inputs other than quoted prices that are directly observable (e.g. interest rates, yield curves, default rates)

- Inputs derived principally from or corroborated by market data by correlation or other means (market corroborated inputs). Example: royalty rates, prices per square foot or valuation multiples.

Adjustments may vary depending on facts and circumstances. Example: condition and/or location of the asset. Significant adjustments may render the fair value measurement a Level 3 measurement

*Level 3:*

-Unobservable inputs:

Inputs derived through extrapolation or interpolation that cannot be corroborated by market data

- o Other entity-specific inputs [historical or projected financial data (revenue, earnings, cash flow, etc.) that are not derived from market data]

- o Unobservable inputs reflect the reporting entity's own assumptions about the assumptions that market participants would use.

- o In developing unobservable inputs, the reporting entity need not undertake all possible efforts to obtain information about market participant assumptions.

The reporting entity must not ignore information about the market participant assumptions that is reasonably available without undue cost and effort.

In the loan origination market, MSRs could be classified as Level 1 Fair Values. Flow and co-issue servicing prices are committed contractual prices from an arms length buyer. In an AOT trade, the MSR value can be directly derived from the total price minus the MBS price. And there is readily available SRP information, which would be argued is a market observable quoted price. Mortgage companies should be able to argue successfully that these MSR prices are a Quoted Price, and therefore, Level 1 Fair Values.

Clearly, Bulk MSRs aren't going to be classified as Level 1 Fair Values because no quoted prices exist. MIAC estimates that approximately 1% to 3% of the entire mortgage servicing assets will trade in the bulk market within a year. These trades are nearly always brokered and everyone would agree that there is no quoted price for a bulk MSR asset.

The MIAC process for independent third-party pricing of a particular portfolio of Bulk MSRs is to map the representative portfolio components to similar benchmark servicing assets, where price discovery can be formalized. The similar assets that MIAC uses as benchmark instruments are the Generic Servicing Assets (GSAs™).

The MIAC GSAs undertake a regular virtual auction process with the largest MSR market participants and are priced by MIAC on a daily basis. GSA's daily prices are published on MIAC's web site, [www.MIACAnalytics.com](http://www.MIACAnalytics.com) and a representative sample is published daily at [www.nationalservicingnews.com](http://www.nationalservicingnews.com) and on a weekly basis at [www.americanbanker.com](http://www.americanbanker.com). MIAC believes that GSAs will serve an important role in helping mortgage companies establish Fair Values for MSRs. In subsequent MIAC publications, MIAC will elaborate further on how GSAs will enable mortgage companies to defend their bulk MSRs as Level 2 Fair Values.

The SFAS 157 also states that "the reporting entity must not ignore information about market participant assumptions that is reasonably available without undue cost and effort." The cost of a GSA subscription

is insignificant and their prices are easily available. MIAC believes that the GSA pricing will continue to gain wide acceptance in the mortgage banking industry and address this SFAS 157 requirement.

Principal (or Most Advantageous) Market:  
Highest and Best Use Analysis:  
Blocking Factor:

All of these SFAS 157 requirements are related to the market execution mechanisms for selling MSRs. The Fair Value measurement must include a disclosure of the assumptions surrounding the market execution mechanisms. Once the assumed market transaction procedures are disclosed, the MSR holders will not need to regularly update these descriptions of the market practices. In addition to a detailed description of the auction procedures, standard representations and warranties, prepayment lock-out protection, due diligence procedures, and MSR transfer mechanics need to be described and their effect on the Fair Value need to be quantified. Independent third-party MSR valuation firms will typically provide this disclosure description and analysis.

Moreover, the MSR holders most likely will be required to obtain an independent third-party description of the standard market practices and an analysis that the assumed market transaction practices represent the *Highest and Best Use* of the asset. The analysis of Highest and Best Use of the asset will include a justification of whether the asset "would provide maximum value to market participants principally through its use in combination with other assets as a group (highest and best use is "in-use")" or "principally on a stand-alone basis (highest and best use is "in-exchange")".

Because MSR acquirers typically assume their marginal cost to service a new portfolio in their bidding process, expect to leverage cross-selling opportunities in their ancillary income assumptions, and often assume different success rates with their retention programs, an "in-use" valuation will likely be the practice of MSR holders.

The statement also allows MSR holders to disclose their in-use fair values as adjustments to in-exchange fair values. The statement indicates, "The in-use valuation premise might be incorporated in the fair value of the asset through adjustments to the value of the asset in-exchange." Clearly, the new Fair Value disclosures will make more explicit the valuation premises to readers of their financial statements.

Expanded Disclosure and Model Input Assumptions:

SFAS 157 will require that the much wider scope of the model input assumptions be disclosed, including the primary components of the valuation models such as the term structure model parameters, prepayment model parameters and types, the source and magnitude of the discount rates or spreads, and the mechanics for assumption and price discovery. Particular scrutiny will likely be placed on the "unobservable inputs (Level 3)". For changes in these inputs, the statement will require a reconciliation of the effects on the Fair Value due to changes in the sig-

nificant inputs and changes "in the observability of significant inputs". Moreover, the "Valuation Techniques" must be categorized as "market approach", "income approach", or "cost approach".

Conclusions:

MIAC believes that SFAS 157 will have sweeping implications directly for how the Fair Value of MSRs are derived and disclosed. The world of running an internal black-box MSR valuation model will soon be replaced with new parlance such as Exit Price and Fair Value Hierarchy. With SFAS 156 requiring the MSRs to be initially booked at Fair Value, whether a buyer and holder of MSRs or a seller of MSRs, both parties will need to fully understand the implications of how the new SFAS 157 Fair Value standard will affect their business practices. The implementations of this new standard will be complex and challenging and, for those most attuned to the details, will represent an opportunity to structure their business practices to most successfully benefit from this brave new world.

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## Banker to Broker?



By Tina Reid, CFA  
SVP, Secondary Solutions Group

In the mortgage biz, moving from broker to banker is often considered a rite of passage. For many, it's a strategic decision that says, "We're ready to play with the big boys now."

And there are significant advantages. As a banker, you can control your own underwriting and closing process. Create your own product set and guidelines, and sell directly to the Street or conduits. You can set your own rates and manage your own rate lock policies. And you can generally get better price execution by hedging your own pipeline (or using a hedge advisor) and selling into bulk, AOT, or mandatory

trades instead of best-efforts.

But in recent months, smaller firms have been forced to reconsider the costs, and risks, of the decision to move from broker to banker. And because the reasons are so compelling in this market environment, even larger firms should consider borrowing from the broker's playbook to reduce the risk in some segments of the business.

**Reason #1: The Market Can, and Will, Reprice Credit Risk**

Many bankers have learned the hard way that the market can reprice credit risk very quickly...too quickly to unload product that

is already in pipeline or sitting in the warehouse waiting for bulk sale. As spreads have widened substantially on Subprime, Seconds, and higher risk segments of the Alt-A market, lenders have suffered substantial losses in the last six months. As a result, many have been forced to close their doors. Others have simply abandoned Subprime and tightened credit standards on Alt-A and Alt-B.

Unfortunately, the highest origination margins are in those higher-risk products, so cutting those product lines means big revenue losses that may be impossible to make up in the A-paper business. Adding to the problem is the fact that margins are shrinking in A-paper from their already slim levels. More and more lenders are turning their focus to A-paper, at a time when the real estate market is suffering and there are fewer and fewer new A-paper lending opportunities.

One alternative to abandoning the higher-risk business is to move to a best-efforts delivery strategy for these loans. Using a best-efforts lock, even at a slightly lower price, will give protection against the possibility that credit spreads will widen further. And although many believe that spreads have already widened as far as they are going to go, the fact of the matter is that a wave of subprime defaults is very possible over the next year, which could cause credit spreads to widen even further. By going back to best-efforts, you can lock in your gross margin at origination and avoid this potential risk.

### **Reason #2: Bulk Bids May Not Beat Investor's Rate Sheet Pricing**

Incredibly, over the last few months, we are seeing lenders actually get LOWER bulk bids for their high-risk product than they can get for selling loan-by-loan to investor's rate sheets. As traders have been getting pummeled by widening spreads, and investors are getting slammed with early payment defaults, skittish buyers are actually paying less in some cases for closed-loan bulk trades than they pay for loans one at a time.

The reason for this may be that the loan-

by-loan process gives the investor a greater opportunity to review and approve each file before they purchase the loans, versus a bulk process that often involves only a due-diligence sampling.

Whatever the reason, rate sheet pricing (whether mandatory or best-efforts) must be taken into consideration in this market. Even if you choose to stick to a bulk sale strategy, be sure to do a loan-level best-execution analysis of your product to all of your investor rate sheets on the same day you hold your auction. This puts a "floor" price on your auction and if the auction results are poor, you can always go back to the posted rate sheets.

### **Reason #3: Just Because You Sold it Doesn't Mean You're Off the Hook**

Many lenders are being reminded the hard way that buyers can, and will, exercise their right to force the repurchase of a loan. When bankers sell closed loans, there is nearly always the risk of repurchase for fraud, misrepresentation, or error.

While the good times were rolling in the real estate market, defaults often cured through sale or refinancing, as rapid property appreciation provided equity to give homeowners more options. Loan buyers were less aggressive in forcing buybacks of defaulted loans, as default losses were generally at or below expectations.

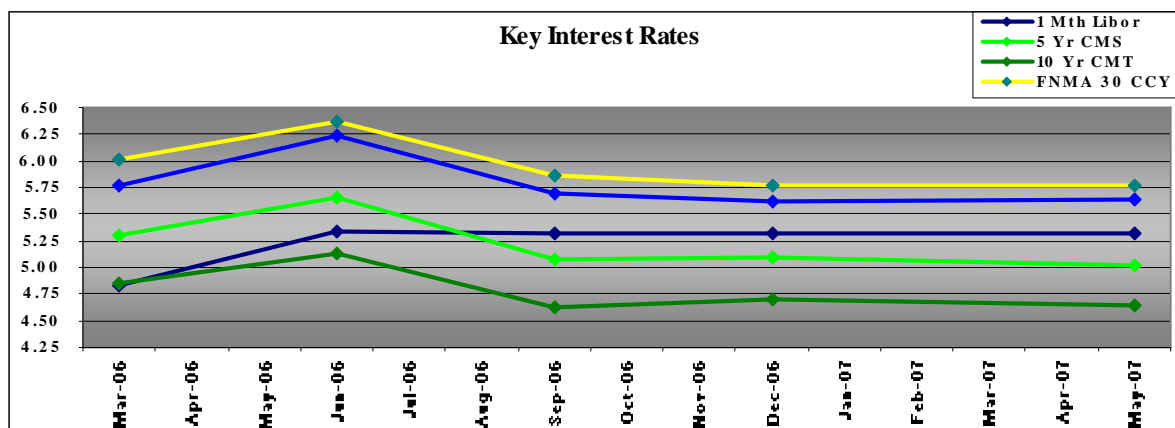
As defaults have increased over the last year, investors are getting more aggressive in pushing defaulted loans back to the originators. And even if your origination shop follows all the rules, you can still suffer. Employment fraud and income misrepresentation, the "little white lies" borrowers tell to qualify for stated-income loans, can result in permanent liability to the originating lender. Inflated appraisals are common, and even if they aren't, "retroactive appraisals" performed months or years after a loan is originated can produce a solid

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# In the Numbers

## MSR Market Update

The MSR Market did not show much volatility during the first quarter of 2007. Mortgage rates stayed in a very tight range during this period, with the 30 Year Fixed Rate Freddie Mac Survey Rate Benchmark settling into a range of 6.16% to 6.30%.



Prime Conventional Prepayment speeds remained in the 9% to 15% CPR range for the majority of the 5.50% through 6.50% coupon product. Earning rates were also relatively flat for the quarter, with both the 1-month Libor and 5-year Swap rate holding steady for most of the period.

### Prepayment Speeds

SIFMA Prepayment Speeds	01/02/07		05/01/07
	WAC	PSA	PSA
CONV15_4.0_2003	4.55	146	149
CONV15_4.5_2004	4.96	159	156
CONV15_4.5_2005	5.13	159	158
CONV15_5.0_2005	5.48	173	176
CONV15_5.5_2005	5.90	209	210
CONV15_5.5_2006	5.98	220	232
CONV30_4.5_2005	5.30	150	144
CONV30_5.0_2005	5.64	160	163
CONV30_5.5_2005	5.99	212	203
CONV30_6.0_2005	6.52	324	289
CONV30_6.0_2006	6.40	382	365
GNMA30_5.0_2005	5.50	163	168
GNMA30_5.5_2005	6.00	195	195
GNMA30_6.0_2005	6.50	294	288
GNMA30_6.0_2006	6.50	349	346

In the first four months of 2007 the bid value of our benchmark Generic Servicing Asset (GSAs) portfolio experienced only a slight bit of volatility, but overall the prices were essentially flat from year-end.

To recap, there was a pickup in mortgage rates in January of about 20 bps, and we saw MSR values in the GSA portfolio as a whole rise about 0.18 of a multiple, but then this was reversed by the end of February with a drop in mortgage rates and the GSA portfolio MSR values fell by about 0.25 of a multiple.

Since February-end, rates have been slowly but steadily rising and MSRs have risen back up to be just about where they were as of December-end.

Transaction activity was somewhat muted with most of the trading activity being in small and middle-sized MSR portfolios. One notable trade of \$9 billion of Agency and Alt-A servicing was brought to market in early March. Market participants indicated that the bidding was

GSA Price Multiple

	Apr-06	Jul-06	Oct-06	Jan-07	May-07
Agency 15-Yr	4.92	5.27	4.63	4.69	4.60
Agency 30-Yr	5.62	6.16	5.52	5.69	5.56
Jumbo 15-Yr	4.16	4.59	3.97	4.30	3.84
Jumbo 30-Yr	4.47	5.07	5.08	5.28	5.02
GNMA 15-Yr	4.26	4.37	4.76	4.81	4.59
GNMA 30-Yr	4.69	5.21	4.95	5.06	4.99
ALT 15-Yr	NA	NA	NA	4.27	4.16
ALT 30-Yr	NA	NA	NA	4.46	4.67
H-ARM 3-Yr	NA	NA	NA	2.63	2.59
H-ARM 5-Yr	NA	NA	NA	3.05	3.07

light, especially for the ARM segment and ultimately only approximately \$6.7 billion of the \$9 billion traded, further demonstrating a relatively weak market.

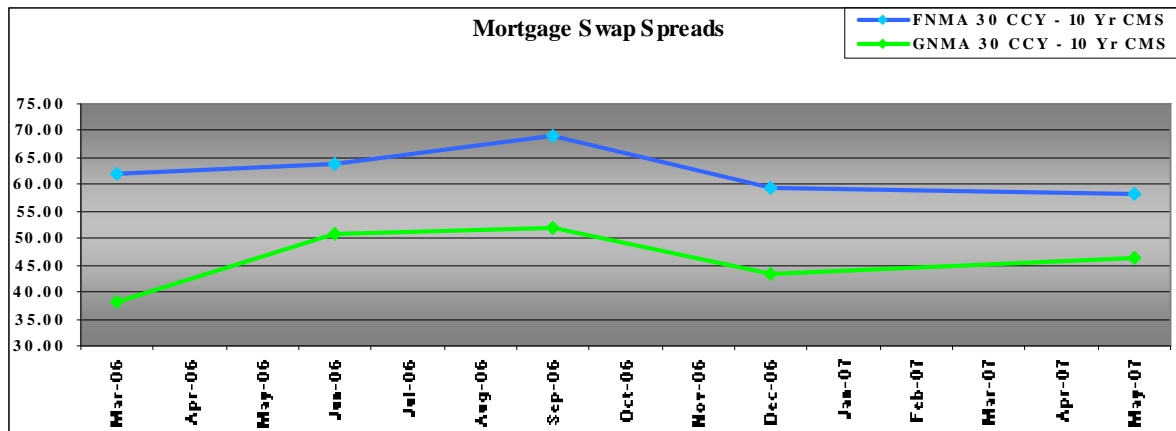
Subprime and Alt-A loans continue to be highly scrutinized by the marketplace. With headline news focused on the weakness in home price appreciation and partially due to lenders applying tighter

origination standards, the more risky sectors of servicing such as Subprime and Alt-A are seeing performance deterioration as a result of many borrowers having a lack of alternatives for refinancing.

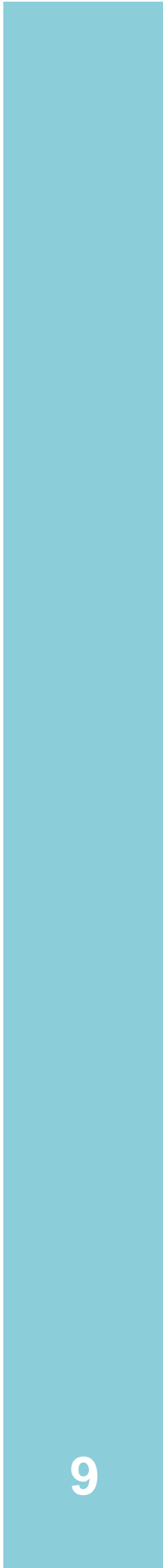
Overall prepayment speeds on this product have slowed substantially compared to earlier vintage pools. The continued reduction in equity takeout situations coupled with longer lead times for selling housing inventory should bode well for a prepayment slowdown over the medium term. A pickup in delinquencies caused by payment reset shocks along with tighter underwriting standards reducing the availability of mortgages for weaker credit borrowers is something that should be closely monitored.

OAS's	01/02/07	05/01/07	
Trust IO's WAC	OAS	OAS	
FHSMB232	5.68	12.2	90.3
FHSMB237	6.04	16.8	114.5
FNMA370	6.43	160.1	186.0
FNMA371	6.94	17.4	-242.3
FNMA353	5.48	-75.5	-54.0

Subprime performance based on recent ABX index reports suggest delinquencies have somewhat stabilized, with a slower pace of increases in total delinquencies. It is safe to assume that on an age adjusted basis, 2006 pool performance on weaker credit pools will be the worst in recent history. However, recent 2007 originated product may have good potential performance based on the tighter origination standards and reduction in leveraged loans.



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argument that the property value was inflated, especially if the property value actually declined after origination. Add that possibility to the weak real estate market we are in right now, and the potential buy-backs are downright frightening.

This repurchase risk is yet another reason to consider brokering high-risk product, or at least, getting prior underwriting approval from your investor for every loan. If the investor made the underwriting decision, the risk generally passes to the investor (check your contract to be sure). And if you allow the lender to close in their name, rather than in your own, you also remove the risk of being on the hook for closing errors, TIL violations and predatory lending lawsuits if a loan goes into default.

#### **Reason #4: Warehouse Lenders Can Be Tough at Times**

It's what I call adding insult to injury. Over the last six months, lenders have often suf-

*"Remember that the decision to be a banker or broker does not have to be an all-or-nothing choice."*

fered severe cash flow problems as high-risk loans generated unexpected losses on sale. Then they get the phone call...their warehouse lender is exercising the right to require a bigger haircut, or worse...disqualifying certain collateral altogether. While you are trying to figure out whether there will be enough cash to make payroll, you learn you have until noon Tuesday to come up with \$5 million. This is when you wish you had taken Mom's advice and become a pharmacist.

The inability to come up with the capital needed to support warehouse lines has been the death blow for many lenders, large and small, in this credit-tightening phase of the cycle. While it is too late for them, you can protect yourself from this

possibility by keeping the highest-risk product off your warehouse line...by brokering it on a table-funded basis, or by getting it off your line as soon as possible, by selling them loan-by-loan and temporarily abandoning an aggregation strategy.

#### **Reason #5: Negative Carry Can Blow a Great Execution**

Volume is down and it is taking you longer to accumulate enough loans for a respectable bulk sale. Not only is this slowing your warehouse turn time and cash flow, one look at the yield curve reveals that you aren't generating the warehouse income you used to...or worse, some segments of your pipeline actually have negative carry. Every day you have to hold those loans you lose a little more.

It is always important to consider interest carry in your best execution decisions, but in a negative carry environment, it is even more critical to do so. In an extreme example, a teaser rate Option ARM loan may generate 6% negative carry, or 50 basis points if you only hold it for one month.

#### **Reason #6: Overhead Costs Add Up**

Let's face it...we are in the downside of the mortgage banking cycle and it may take a year or two of consolidation before we get into a growth environment again. For smaller mortgage bankers, downsizing to a simplified, sales-focused strategy may be the answer. Brokering loans removes the need for most underwriting, closing and secondary marketing staff. For some firms, this may make the difference between surviving the remainder of this downturn or going out of business.

#### **It Doesn't Have to be an All-or-Nothing Decision**

As you assess your strategic options for weathering this storm, remember that the decision to be a banker or broker does not have to be an all-or-nothing choice. The benefits of being a mortgage banker are significant, but the risks should be weighed independently for each product line. Brokering higher-risk loans may allow you to continue to enjoy the higher origination margins on these loans, while significantly reducing your secondary market risk.