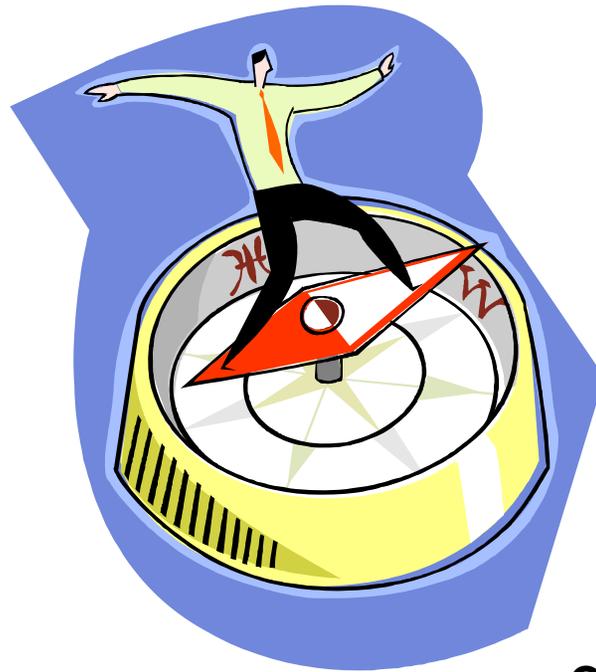


Residential Lending

"Changing Directions"



Community Banker Conference

October 25, 2007

Federal Reserve Bank of Boston

Andrew Olszowy

Manager - Consumer Compliance Team

Residential Lending

Then, Circa 1990....

- Homogeneous Products
- Securitization - Fannie / Freddie
- Lenders / Brokers - smaller players
- Technology - (HP12c?)
- Subprime?
- Regulatory Issue - Equitable Access to Credit

Residential Lending

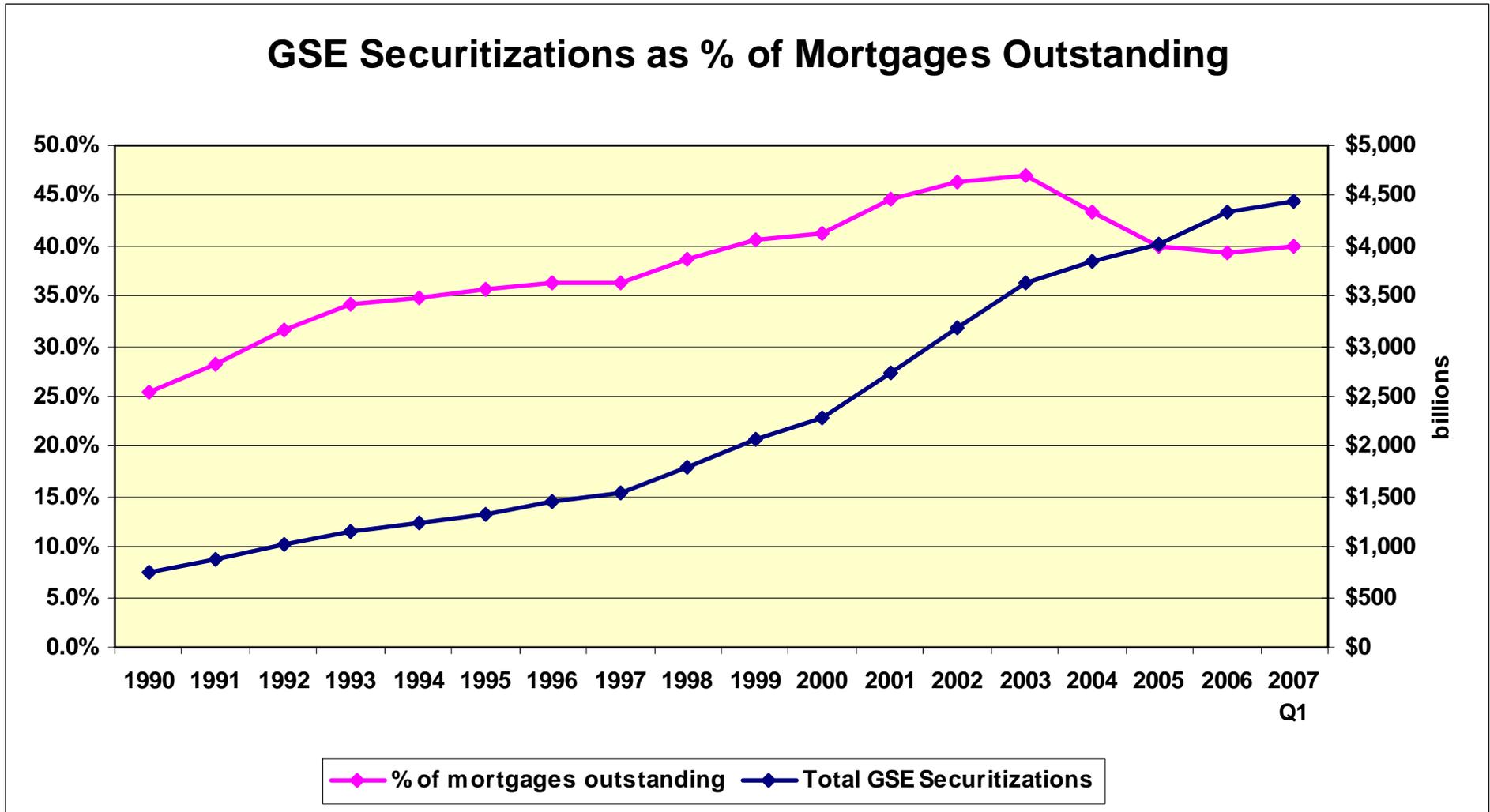
Now - 2007.....

- Diverse Products
- MORE Securitization - Private Label
- Lenders / Brokers - significant players
- Robust use of Technology
- Subprime!!
- Regulatory Issue - Too Much Access to Credit?

Securitization

- Frees additional capacity - lenders lend more, people borrow more.
- Fuels the broker / lender boom.
- Model - "Take Deposits - Make Loans" becomes "old school."
- Securitization removes credit risk (ha ha!)

Securitization



Source: OFHEO

Brokers / Non Bank Lenders

- Brokers have access to multiple investors - provides pricing flexibility.
- Improving technology allowed better pricing tools, faster credit decisions, and risk based pricing.
- Incentive structures creates a more "eager" originator.

Brokers Become Big Players

Two Takes on Broker Originations

According to a 2004 study by Wholesale Access Mortgage Research & Consulting, Inc., there are approximately 53,000 mortgage brokerage companies that employ an estimated 418,700 employees and originated 68% of all residential loans in the US in 2003.

All Loans - 2005 H2	
Retail	45%
Direct - Internet	2%
Direct - Other	3%
Broker	50%
Subprime Only - 2005 H2	
Retail	27%
Direct - Internet	1%
Direct - Other	1%
Broker	71%

Source: Mortgage Bankers Association

Technology

- DU and LP "brings the bank" to the borrower.
- Internet based banking allows for a 24/7 application process

Technology

2007 MortgageBot Study

Review of online lending practices and procedures implemented at more than 3,600 mortgage-lending websites maintained for its more than 700 clients nationwide.

- The study showed that a **quarter** of the lenders studied "now originate **more than half** of their loan volume via the online channel."
- Mortgagebot cited an August 2006 Forrester report showing the Internet as the fastest-growing channel for mortgages, with 70% of loan seekers going online to shop for rates.

Source: American Banker

Heavy Use of Internet Advertising

- Mortgage Lenders continue to advertise heavily on web.
- Nielsen/NetRatings Top 10 Web advertising included four mortgage/financial advertisers from August, 2007.
- Three increased ad budgets --
 - ▲ Countrywide Financial, which increased ad spending from \$34.8 to \$35.4 million.
 - ▲ Low Rate Source
 - ▲ InterActiveCorp (parent of LendingTree.com), and
 - ▼ Experian

Internet Advertising

Top 10 Advertisers by Estimated Spending (U.S.)

Advertiser	Total Estimated Spending	Impressions (000)
1. Low Rate Source	\$51,670,100	25,076,624
2. NexTag, Inc.	\$49,627,300	23,614,378
3. Experian Group Limited	\$40,895,600	14,891,457
4. InterActiveCorp	\$35,537,500	8,842,437
5. Countrywide Financial Corporation	\$35,442,800	17,380,341
6. AT&T Corp.	\$29,774,300	10,748,844
7. Netflix, Inc.	\$29,691,100	9,071,800
8. Verizon Communications, Inc.	\$19,487,900	4,949,850
9. Monster Worldwide, Inc.	\$17,355,500	3,264,426
10. Privacy Matters	\$14,336,600	4,728,581

As of August 2007

Source: Nielsen

Internet Marketing

CNNMoney.com

GET QUOTES SYMBOL LOOK-UP **SEARCH** Entire Site

HOME NEWS MARKETS MY PORTFOLIO TECHNOLOGY JOBS PERSONAL FINANCE LUXURY **REAL ESTATE** SMALL BUSINESS RANKINGS

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REAL ESTATE

Mortgage Meltdown 2007 [+ Archive](#)

Mortgage resets: Record bill coming due

Billions in subprime ARMs will be subject to higher payments.

By **Les Christie**, CNNMoney.com staff writer
August 13 2007: 11:45 AM EDT

NEW YORK (CNNMoney.com) -- More than two million subprime adjustable rate mortgages (ARMs) are poised to reset at much higher rates in coming months, worsening an already suffering housing market.

Borrowers who took out hybrid ARMs in 2004 and 2005 to secure low "teaser" rates for the first two or three years of the loan may see their monthly mortgage payments climb by 35 percent or more.

Consumer groups and politicians worry that hundreds of thousands of subprime ARM borrowers will be unable to keep up with their mortgage payments and will lose their homes.

"In October alone more than \$50 billion in ARMs will reset," according to Mark Zandi, chief economist and co-founder of Moody's Economy.com. That's a record, according to Zandi.

Bankrate.com

Type	Overall avgs
\$30K HELOC	7.88%
\$50K HELOC	7.77%

Top Stories

- [100 Fastest-Growing Companies](#)
- [Fuzzy Bush math](#)
- [Stocks seek higher ground](#)
- [Subprime woes weigh on job outlook](#)
- [Manufacturing slows in August](#)

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Protect them with Life Insurance

AGE MALE 35 \$16.53 **CLICK HERE**

Web Advertising

Foreclosures: Hardest hit zip codes

A buyer in 2005 with poor credit and limited means might have signed on for a \$200,000 2/28 hybrid ARM, locking in a fixed rate of 4 percent for two years. After paying \$955 a month, the bill would now be set to spike to \$1,331, a 39 percent increase.

Until recently, rising home prices bailed out many ARM borrowers in trouble. They could raise cash with cash-out refinancings or home equity lines of credit. If worse came to worse, they could sell the house and get some money back.

But prices have stabilized or slipped in many markets. ([Latest home prices.](#))

As a result, Doug Duncan, chief economist for the Mortgage Bankers Association (MBA), is expecting as many as 600,000 home owners will get into trouble with perhaps half of them actually losing their homes.

One of the reasons for the worsening situation, according to Zandi, is that just as the number of subprime ARMs being underwritten was reaching a high, the quality of loans was hitting new lows.

"There were increasingly poor quality loans made starting in the spring of 2005," he said, "with the poorest of all made during the fall of 2006."

\$30K Home Eq	8.52%
\$50K Home Eq	8.47%
\$75K Home Eq	8.34%

Find personalized rates:
Enter ZIP code

Sponsored Links

House Payments Fall Again

\$310,000 Mortgage for \$999/Mo. Paying too much? No credit check reqd.

Hot Stock Alert

Gulf Ethanol Corp (OTC: GFET). Ethanol, Biofuels, Green Energy. www.GulfEthanolCorp.com

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The Home as an ATM?

- Nationwide home appreciation coupled with ongoing favorable rate environment had people tapping into home equity like never before.
- A "mortgage" becomes, for the first time, not something you have to get, but something you want.

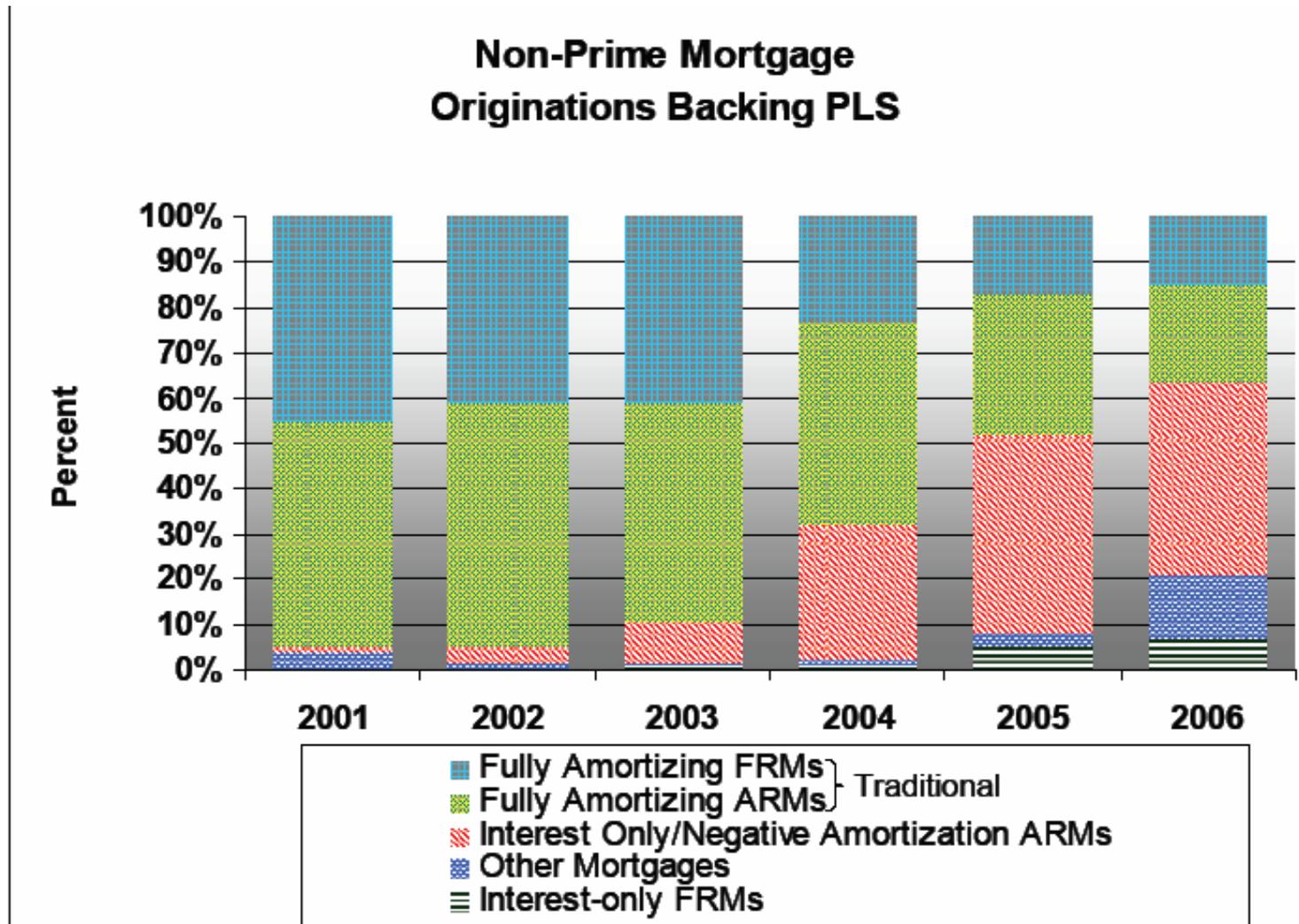


Everybody Wants Some!

...or how subprime explodes.

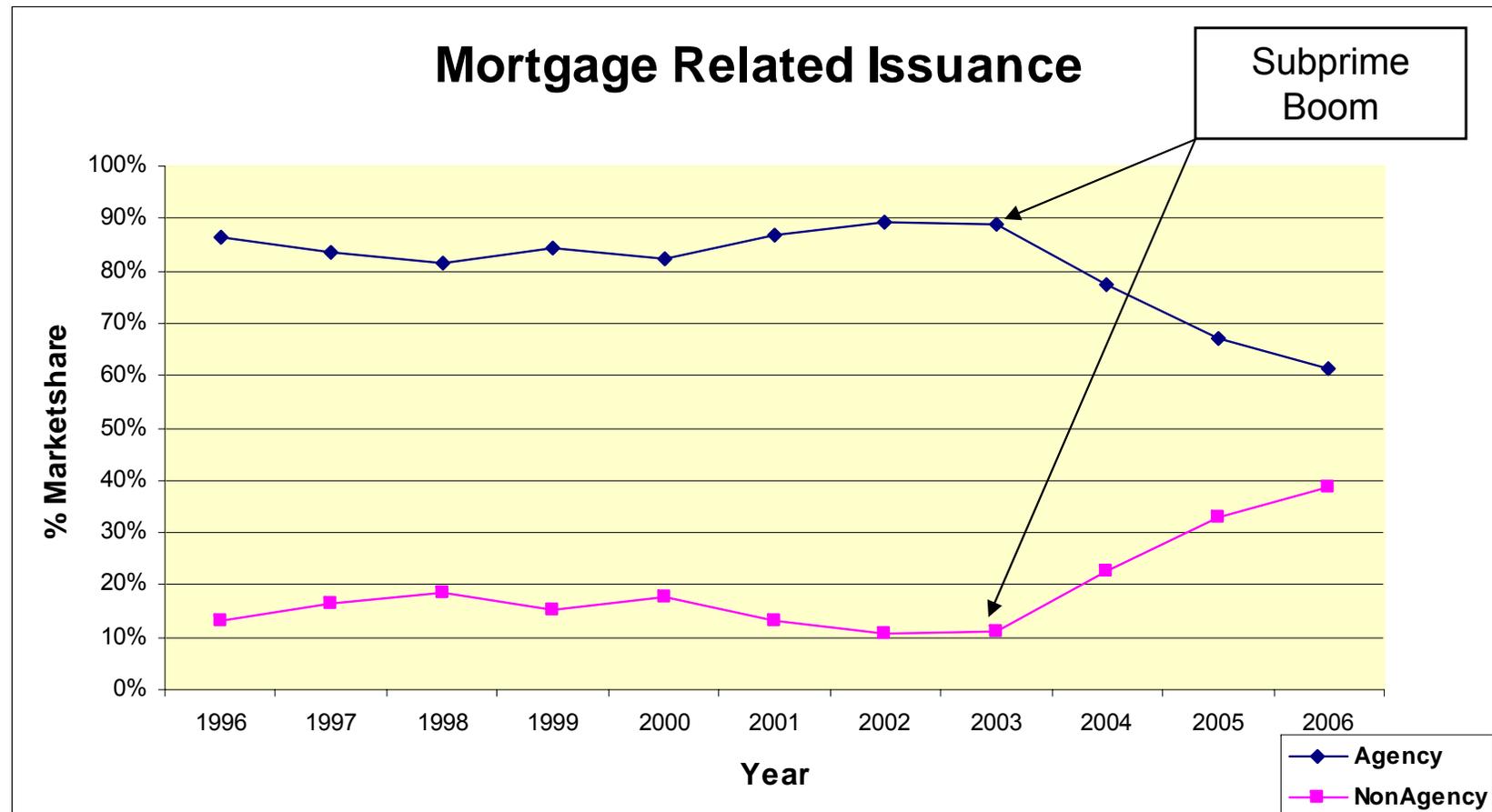
- **Consumers** want to tap into their home equity.
- **Brokers/Lenders** want the fee income from the now frequent refinances.
- **Investors**, eager to take advantage of the US real estate market, tap into the higher yielding subprime tranches.

Subprime Originations



Subprime and Private Label

1996 - 2006



Source: Securities Industry and Financial Markets Association

Who Buys MBS?

Investor Type	2002		2003		2004		2005		Midyear 2006	
	\$ bn	% of Total								
Commercial Banks	702.1	19.6	775.6	19.4	876.4	19.6	897.1	17.3	969.8	17.8
Thrifts	209.7	22.4	206.5	5.2	234.3	5.2	242.6	4.7	242.9	4.5
Federal Credit Unions	25.2	2.7	28.5	0.7	27.5	0.6	54.5	1.1	70.5	1.3
Total Depository	937.0	26.2	1,010.6	25.2	1,138.2	25.4	1,194.2	23.0	1,283.2	23.5
FNMA/FHLMC Portfolio	1,109.4	31.0	1,232.5	30.8	1,260.9	28.2	1,123.2	21.6	1,150.0	21.1
Foreign Investors	235.0	6.6	285.0	7.1	490.0	11.0	802.0	15.5	850.0	15.6
Mutual Funds	375.0	10.5	387.0	9.7	375.0	8.4	405.0	7.8	400.0	7.3
Personal Sector	120.0	3.4	200.0	5.0	235.0	5.3	355.0	6.8	360.0	6.6
Life Insurance Cos	235.0	6.6	240.0	6.0	265.0	5.9	285.0	5.5	300.0	5.5
Public Pension Funds	95.0	2.7	120.0	3.0	152.0	3.4	180.0	3.5	190.0	3.5
Private Pension Funds	90.0	2.5	105.0	2.6	115.0	2.6	160.0	3.1	175.0	3.2
FHLB	96.4	2.7	97.9	2.4	113.1	2.5	122.3	2.4	127.8	2.3
Securities Brokers/Dealers	40.0	1.1	35.0	0.9	50.0	1.1	95.0	1.8	115.0	2.1
REITs	12.7	0.4	28.6	0.7	79.0	1.8	107.4	2.1	112.1	2.1
Depository & Major Investors	2,408.5	67.4	2,731.0	68.2	3,135.0	70.1	3,634.9	70.0	3,779.9	69.3
All other Investors*	230.2	6.4	261.9	6.5	201.2	4.5	360.0	6.9	387.5	7.1
Total Outstanding	3,575.7		4,003.5		4,474.4		5,189.1		5,450.6	

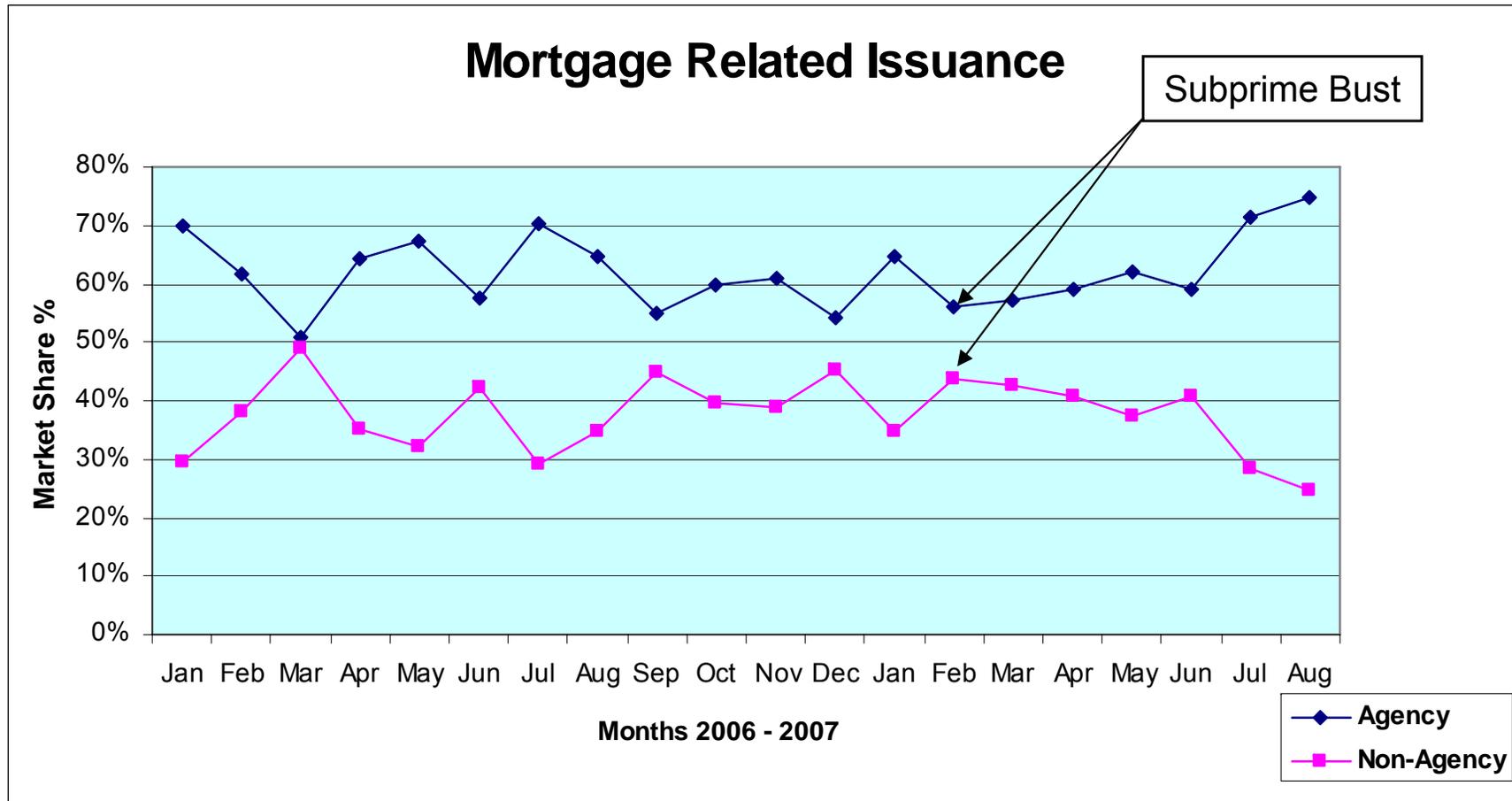
Notes: Mortgage-related securities, include all securities or debt obligations collateralized by either residential mortgages. Estimates are in italics and from Inside MBS & ABS based on available Federal Reserve Board data.

*Other investors include hedge funds, nonprofits, other groups, property/casualty insurers, and state/local government where MRS data is not available.

Table from UBS Presentation dated May 22, 2007

Subprime and Private Label

January 2006 - August 2007



Source: Securities Industry and Financial Markets Association

So Why is This Important to New England Community Banks?

New England Community Banks are Heavy Residential Lenders

- Of top 150 community banks with largest first mortgage portfolios, 60 are New England banks as of 12/31/06
- Of those top 150 banks, New England banks own 43.1% of all the first mortgages held.
- NE has 13 of the top 22 institutions

Source: SNL Financial

New England is Heavy in Savings Banks

Top 10 States Ranked by % of Savings Bank Deposits

2006

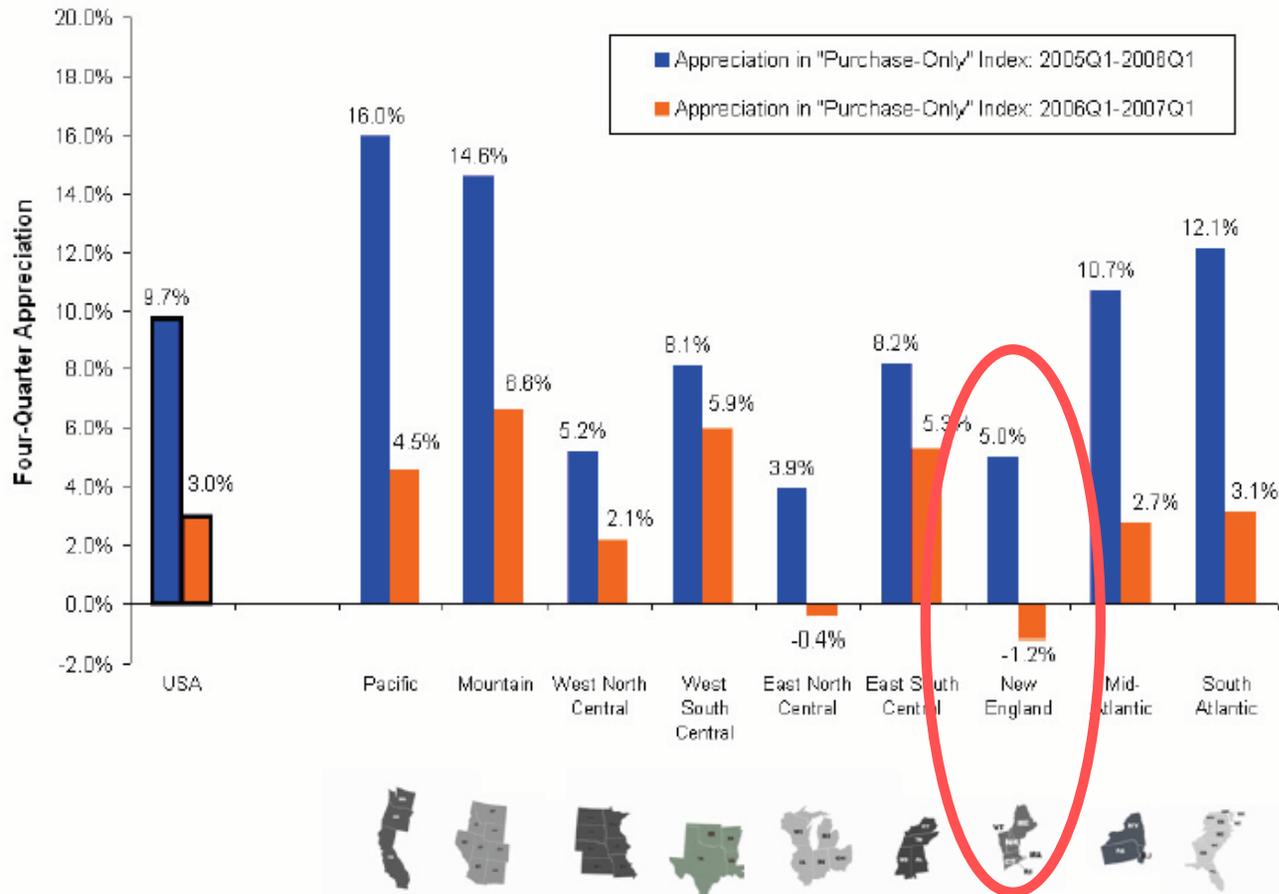
Connecticut	\$	18,912,679	22.3%
Maine	\$	4,486,579	19.5%
Massachusetts	\$	28,021,388	16.7%
New Hampshire	\$	1,785,085	7.6%
Rhode Island	\$	1,302,007	5.3%
Pennsylvania	\$	9,227,218	3.5%
Delaware	\$	535,471	2.8%
New Jersey	\$	4,513,425	2.1%
Alaska	\$	205,374	2.0%
Washington	\$	2,302,849	1.9%
US	\$	105,524,984	1.6%

* dollars in 000s

Source: SNL Financial

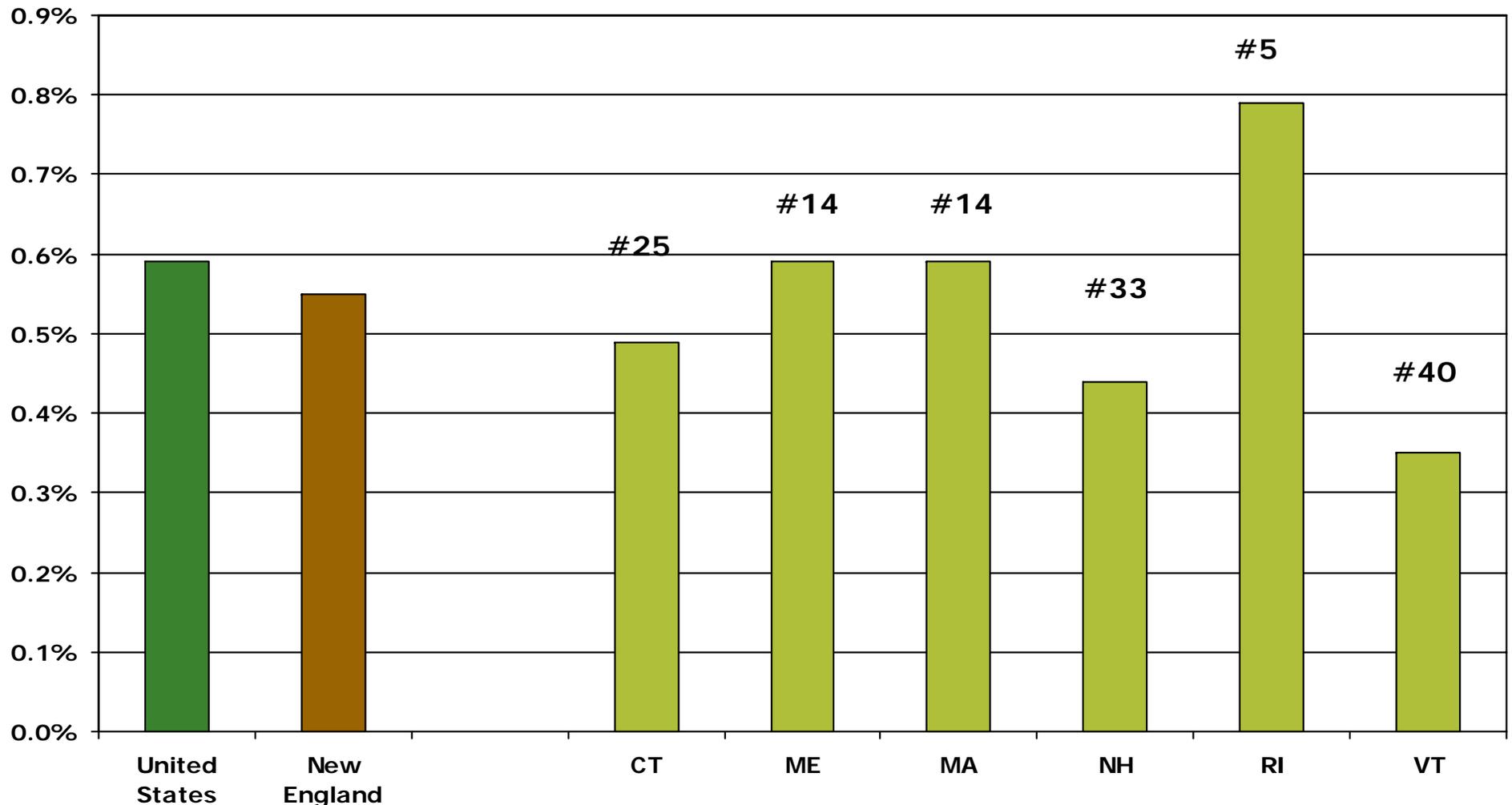
National Housing Appreciation Rates

**FOUR QUARTER APPRECIATION RATES:
MOST RECENT YEAR vs. PRIOR YEAR**



7

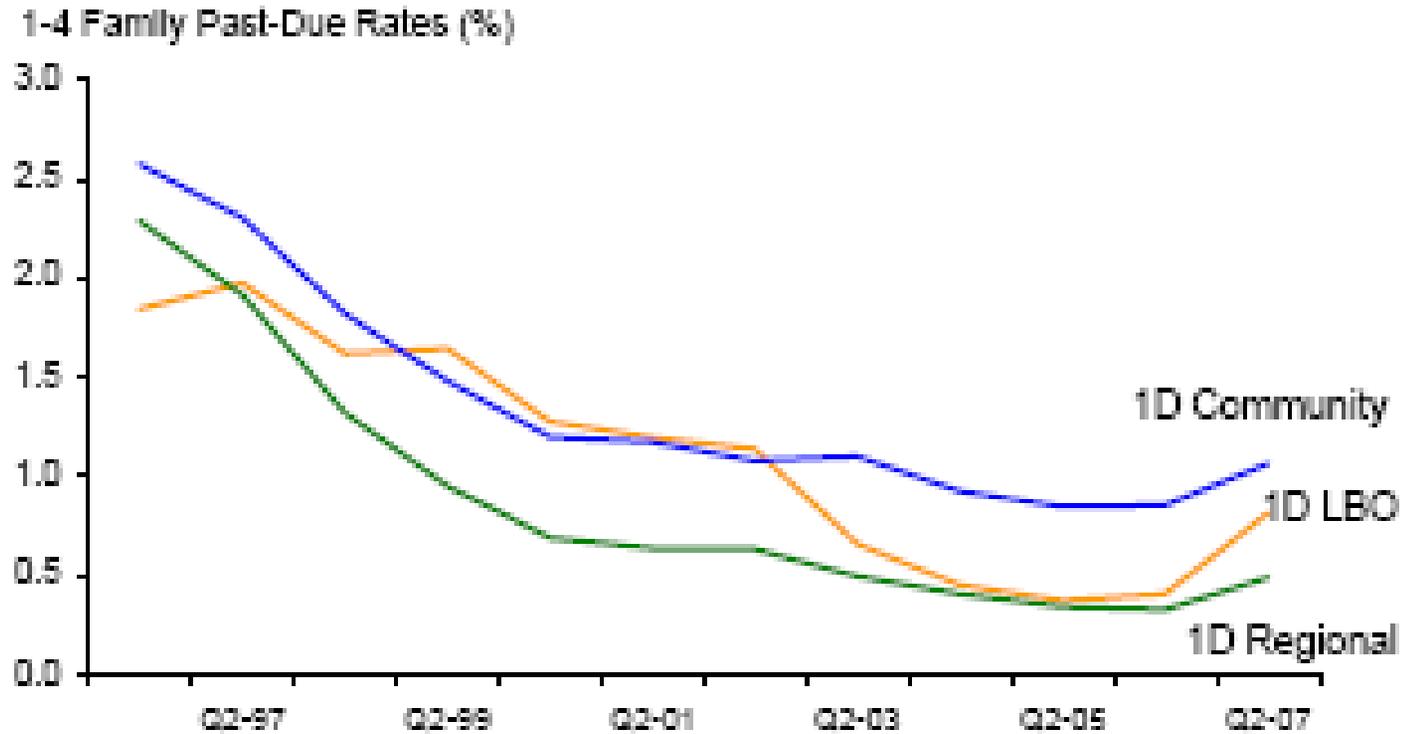
Rhode Island now has 5th-highest foreclosure rate in country. The highest state foreclosure rates is MI, down to 1%; ND has the lowest at 0.2%.



First District Experiences

1-4 Family Past Due Rates

The good news, is delinquency rates are still relatively low



Source: Bank Call Report

First District Experiences

- Home mortgage business volume is down.
- Secondary market underwriting standards have not changed.
- Real estate market is the pressing concern.
- Some consumer pullback due to subprime.
- Increasing commercial mortgage activity.
- May be slow going for home mortgage lending.

Fed Subprime Study

- All subprime loans made in Middlesex County, MA
- 1992-2006, over 2 million loans
 - 30% of subprime hold more than one property.
 - 18% subprime borrowers have credit scores over 700.
 - Many may have held on long enough for property to appreciate.
 - "Teaser" rates (2/28s and 3/27s) not so much of a teaser
2005 average - 7.3%, 2006 average - 8.35%.
 - 15% in default, but 85% are good.

First District Experiences

Mortgage Lenders Report

- Subprime has dried up.
- Investor pool is much smaller and are looking for "prime" underwriting standards.
 - This coupled with soft RE market has made it hard to originate any loans
 - Difficult to originate subprime loan to applicant with a 680 credit score.
- Good news - resets may not be as bad as originally thought.
- Still - this is not good news.

Community Banks Not Immune

- Pressures are real!
 - NIM Compression
 - Core Deposit Gathering
 - Earnings Pressure
- Subprime was tempting
 - Creativity is key!
 - 3rd Party relationships
- NetBank - \$2.5 billion bank shut down 9/28/2007 due to mortgage losses and early payment defaults.

First District Experiences

One bank's story....

- Business volume is up.
- Originate to sell on secondary market (conforming)
- Underwriting standards have not changed.
- Subprime situation has redirected potential borrowers from mortgage companies to banks.
- It's *the ability to repay*.
- Business as usual.

Silver Lining?

- Overall, community banks are sitting tight
- Jumbos – bank niche product?
 - Banks competitive:
 - ½ to 1 point lower than mortgage lenders.
- Portfolio lenders – good prognosis
- Funding sources – remain solid
- Advertising trends – banks exploit *stability*.
- Rebuilding market share.

Questions?

