Election Results Push Rates Down; M&A Trend Rolls On; Increased Regulations Ahead; Ocwen, Nationstar, Zillow Stock Movements

By: Rob Chrisman | Wed, Nov 7 2012, 11:12 AM

Usually I put the bank, M&A, investor, and agency news down lower. But today I am putting it here - **the trends in M&A are unmistakable** as companies band together for various reasons, not the least of which is sharing increased compliance and regulatory costs.

First Republic Bank, a private bank & wealth management company (and frequent contributor to Redwood Trust jumbo deals), announced that Luminous Capital Holdings, LLC, one of the nation's leading independent wealth advisors will become part of First Republic Investment Management.

KBW, who was itself acquired, announced that Nasdaq-traded companies **PacWest Bancorp and First California Financial Group** signed a definitive agreement and plan of merger. First California (not the California wholesaler) is the parent of First California Bank and had approximately $2.0 billion in assets and 15 branches across Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo and Ventura Counties.

Keefe, Bruyette & Woods also announced another merger on the other coast: **New Traditions National Bank will become a subsidiary of Old Florida Bancshares, Inc**., which owns and operates Old Florida National Bank and Mercantile Capital Corporation.

But "the hunter became the hunted" when boutique investment bank **Stifel Financial announced the $575 million acquisition of KBW Inc**. (KBW), making this Stifel's 10th purchase since 2005. KBW operates the Keefe Bruyette & Woods broker dealer. Stifel has been busy in recent years, acquiring Legg Mason's capital-markets business and Thomas Weisel Partners Group. It was among the companies that bid on all or part of bond-trading firm Gleacher & Co., according to press reports.

Lastly (for now) in Kansas **Bank of Hays ($204mm) will buy Farmers' State Bank** of Jetmore ($26mm) for an undisclosed sum.

Fifth Third reminded clients that all HARP 2.0 loans with LTVs that exceed 105% must be delivered by November 30th and funded by December14th.

For all self-employed borrowers with loan applications dated October 20, 2012 or after, Fifth Third is requiring the most recent two years' signed tax returns as verification of income, regardless of AUS findings.

Beginning November 5th, **Flagstar** began requiring all loan files to contain a copy of the Undisclosed Debt Acknowledgement and will be auditing files to ensure its inclusion with the underwriting and post-closing documentation.

Flagstar is allowing the use of Hardest Hit Funds for HARP loans provided that they don't result in a recorded lien on the property and are used to pay down or curtail the outstanding balance on a borrower's existing loan and/or associated financing costs. The file should contain documentation that verifies the terms and conditions of the HHF funds, which should be disclosed on the HUD-1 and included in the monthly DTI ratio upon repayment unless repayment is due only upon sale or default. Currently, the HHF funds are available only in Arizona and Nevada, but other states' HFAs are expected to get theirs rolling in the near future.

M&T Bank began pricing its new SONYMA Conventional Plus loans in the correspondent channel for New York properties on October 22nd. The program is based on Fannie's MyCommunityMortgage and offers 30-year fixed-rate loans that can be partnered with SONYMA's Down Payment Assistance Loans (DPALs) as an alternative to FHA financing. In addition to potentially lower monthly payments, borrowers can benefit from further savings if they're eligible for a SONYMA-issued Mortgage Credit Certificate, which allows them to convert 20% of their annual mortgage interest into a tax credit. The SONYMA Conventional Plus program isn't restricted to first-time homebuyers, doesn't have purchase price limits, and doesn't qualify based on household income, unlike traditional SONYMA programs. Participating lenders must be SONYMA-approved and must execute a tri-party agreement with SONYMA and M&T.

All M&T properties in the Florida counties affected by Hurricane Isaac whose appraisals were completed before August 27, 2012 must be re-inspected as per the disaster policy. The original appraiser should complete the inspection and must include exterior photos, confirmation that the property hasn't damaged, and commentary on conditions that may affect the property's marketability.

Back to trivia - like the **election results**! Elizabeth Warren, the CFPB architect and frequent bank critic, was elected to the Senate, much to the dismay of the financial services industry, and we all know about Barack Obama's victory.

"Rob, don't you find it somewhat intriguing that one of the most important and critical actions we as Americans partake in is voting for of all things a President. At the same time we hear about the regulators bearing down on us and forcing us to upgrade our LOS's, due to new regulations. **Isn't it somewhat puzzling that so many voting machines under the care of government are failing**, not responding and causing millions in legal minutia as they are asked to perform the simple task of scanning a document (something we do all day everyday) or using a touch screen? Compared to a LOS and the tasks we are asked to perform this is child's play!"

Regardless of which politicians won yesterday, the government will still have to deal with the "fiscal cliff" and its profound economic consequences. The market was expecting a knee-jerk reaction to President Obama being re-elected is a rates rally and a sell-off if Governor Romney is elected. This appears to be largely related to what the next president will have to address almost immediately - the fiscal cliff. A quicker resolution is seen with Romney while the acrimony between the Democrats and Republicans suggests a longer time to resolution which would weigh on the economy's growth.

Impacting not only folks in our industry but the whole nation are the longer term issues related to **the housing market, the future of the GSE's including the FHFA leadership, as well as a possible new Fed chairman in 2014, along with their policy actions**. Experts believe that there will be no threat to QE3 under Obama, but that higher coupons are at risk if a new FHFA director comes in who supports principal forgiveness. Yes, Obama (and Elizabeth Warren) won, and banks can look forward to even more regulations and oversight. More

Certainly investors fear that Obama (and Romney, if he won) will struggle to reach a compromise with the leaders of the opposing party in Congress to halt $600 billion in expiring federal tax cuts and automatic spending cuts at year-end. The lack of a resolution could push the world's biggest economy into a deep recession, a consensus view supported by analysts at the Congressional Budget Office. "I think the current situation politically hurts us very badly in trying to deal with our problems economically," veteran bond investor Dan Fuss at Loomis Sayles in Boston said of the so-called fiscal cliff, his No. 1 worry. Neither an Obama nor a Romney win will change Fuss' market outlook. Many warn the Fed is only postponing a destabilizing rise in rates that would hurt economic growth. There's a sense that with Obama's win, the Fed accommodation (QE3) will continue as planned.

Let's take a moment to look at share prices of non-bank mortgage servicers **Ocwen Financial (OCN) and Nationstar Mortgage Holdings (NSM)**. Both sank 5% and 6%, respectively, on Monday in an apparent response to an announcement that MetLife agreed to sell its mortgage servicing portfolio JPMorgan Chase. At this point we know that MetLife is selling its $70 billion mortgage servicing portfolio to JPMorgan, boosting JPMorgan's servicing business by more than 5%.

As an astute reader wrote, "The major reason for the purchases by Ocwen was to move away from the run-off of the subprime servicing portfolio, and expand the FHA servicing portfolio. If you take a look at the moves from the spinoff of Altisource, the purchase of LendersOne (part of C1), after 18 months, a GNMA Seller/Sevicer of both residential and HMBS, and now the purchase of ResCap and Homeward, this will put Ocwen in a long term growth pattern in the GNMA space."

Given the looming threat of Basel III's capital requirements for banks, especially with regard to servicing, non-depositories Ocwen and Nationstar have competed aggressively for mortgage servicing operations as banks lighten up on that business. Last month, Ocwen outbid Nationstar in a $3 billion deal for the mortgage servicing unit of Residential Capital, owned by auto-financier Ally Financial. As noted above, Ocwen also picked up Homeward Residential Holdings last month. Those purchases make it the fifth-largest mortgage servicer in the country, the company said.

Last week, Ocwen reported lower-than-expected quarterly profit. **Nationstar came out yesterday showing a strong origination 3rd quarter**, and a servicing pipeline up to $600 billion. The difference between reported and operating numbers reflected $3.9 million of ResCap and other transaction-related expenses. Total servicing revenues came in less than expected, but this was largely offset by higher origination income and lower operating expenses. The servicing portfolio increased to $198 billion from $193 billion and the gain-on-sale margin increased sharply, and management expects to close $30 billion of UPB purchases this quarter! During the 3rd quarter origination volume of $1.82 billion increased modestly from $1.81 billion in 2Q. However, gain-on-sale (GOS) income increased to $139 million from $102 million on stronger margins. **Analysts suggest that the increased margins reflect the strong lock volume in 3Q of $4.4 billion**, as rate locks are the primary driver of margins. The total application pipeline increased to $5.5 billion from $3.1 billion in 2Q.

Sticking with stock moves, no sooner do we find out that Zillow purchased Nebraska's Mortech than the stock market smacks it. **Zillow posted a record decline** after forecasting fourth-quarter revenue that trailed analysts' estimates. Sales this quarter will be $30-31 million, up from $19.9 million a year earlier. It is good, but lower than the $32.4 million average estimate of analysts, according to data compiled by Bloomberg. Darn that Trulia! (**Trulia**, the online real estate site, went public in September.) But Zillow's numbers are strong, regardless of expectations: revenue in the third quarter jumped 67%, the company swung to a profit by recording net income of $2.33 million after reporting a loss of $570,000 a year earlier. Still, its stock price dropped 18% at one point.

Speaking of market events, as a follow up to a recent Barron's article on **Radian**, folks should check out comments section, where there's a Letter to the Editor posted from a Radian investor.

Tuesday was not a good day for the fixed-income markets. Mortgages "took it on the chin." Dealers reported above average originator selling - locking ahead of the election results perhaps? Traders also saw the FED and a few money managers try to step in and add a few blocks but their buying was not been able to stem the tide. By the end of the day the 10-yr was worse by about .5 in price, closing at 1.74%, and MBS prices were worse by about the same.

But with some uncertainty removed after the election, overnight Treasuries rose, with 10-year yields falling the most in two months as Obama's re- election bolstered speculation the Federal Reserve will stick to its policy of buying bonds to support the economy. After all, **Obama backs government intervention through the Fed's QE3 plan and buying more than $40 billion a month of agency MBS.** The 10-yr. dropped to 1.66%, the lowest level since Oct. 16. Interestingly enough, ever since Lyndon B. Johnson defeated Barry Goldwater for the presidency in 1964, yields on 10-year Treasuries have dropped about 40 basis points in the first month when a Democrat wins, and risen 19 after a Republican victory, according to data compiled by Bloomberg.

This morning we've had the MBA application index for last week, greatly influenced by Sandy. (Who wants to lock in a loan to refinance after their car floated into their living room?) Applications dropped for a 5th straight week, this time down 5% with both purchases and refi's down about 5% - refi's still make up about 80% of industry applications (mostly due to large banks' refi work). Later we'll also have the second leg of this quarter's Treasury Refunding with $16 billion 10-year notes auction at 1PM EST. **But in the early going it is hard to complain much about the 10-yr going down to 1.64% and MBS prices better by about .250.**

A driver is stuck in a traffic jam on the highway outside Washington DC.
Nothing is moving. Suddenly, a man knocks on the car window.
The driver rolls down the window and asks, "What's going on?"
"Terrorists have kidnapped the members of Congress and they're asking for a $100 million ransom! Otherwise, they are going to douse them all in gasoline and set them on fire. We are going from car to car collecting donations."
"How much is everyone giving, on average?" the driver asks.
"Roughly a gallon."

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