

The schedule on the following page was presented by Fannie Mae to one of its lender advisory boards on a conference call conducted on October 18, 2011. One purpose of the call was to update and clarify for the advisory board the status of FHFA's servicing compensation initiative. Participants on the call tell us that Fannie Mae used this schedule extensively to try to support their assertion that servicing consolidation is caused by vastly different economics and accounting between large "price setter" mortgage companies and smaller "price taker" mortgage companies. Unfortunately, their analysis is fatally flawed, full of errors and misstatements, such that we are compelled to prepare this rebuttal.

### ***Lender Assumptions –***

The most egregious misstatements are in the "Lender Assumptions" in the table on the right side. Fannie Mae shows a "Base MSF multiple" of 4.0x for the price setter and 1.9x for the price taker. In fact, both are required by current accounting standards to record their MSR's initially at fair value, which is the same for all market participants. Also, current multiples for initially recording MSR's range in the 4.75x to 5.25 x for new, market rate, 30-year fixed rate mortgages. This information is readily available from MSR evaluators and corporate Form 10Qs, so it's disturbing to see Fannie Mae making up numbers in their analysis.

In their example, for Excess IO Multiple, Fannie Mae uses a 4.0x multiple for price setters versus a 3.4x multiple for price takers. Once again, accounting standards require that this asset be booked at fair value, which is the same for all.

The cost to service ("CTS") differential shown has nothing whatsoever to do with the initial booking of MSR and loan execution and pricing. Fannie Mae seems to be attempting to shore up an already seriously flawed analysis. No competent mortgage originator makes any such adjustment in their loan pricing.

Finally, the G-fee differential is real, but understated in this model. Fannie Mae shows a 4-basis point differential, which does accurately reflect the difference shown in a recent comparison of the top ten servicers to the next 100. However, if you compare the top 4 to the rest, the difference will be a many basis points larger. Prior to 2008, the G-fee differential was even greater and is probably the single most important factor that led to servicing consolidation. Fannie Mae argues separately that lower G-fees for the "price setters" is justified by such things as counterparty risk, yet the largest counterparty exposure is now concentrated in the top four servicers. Looking back at Countrywide, Washington Mutual, Wachovia, IndyMac and others, it's easy to make a case for charging large players a higher G-fee.

### ***Illustrious Summary of Loan Value Differences –***

Turning attention to the table on the left of Fannie Mae's presentation, the values for the differential for CTS, Base MSF and Excess IO multiple should all be zero (0) instead of the numbers made up for this table. That leaves only the G-fee to impact relative execution and pricing. It's as simple as it sounds.

### ***Conclusion –***

The author is fabricating numbers to support a case that isn't supportable. Industry consolidation is the direct result of the decades long G-Fee differentials and the merger of failed mega- servicers required by the mortgage meltdown of 2008.

This simplified illustration is intended to facilitate discussion on the relative differences in lender valuations arising from three often-mentioned factors heard throughout the stakeholder feedback process:

- (i) g-fee differentials,
- (ii) economies of scale (costs to service) differentials, &
- (iii) capitalized MSR (MSF, Excess IO, Float & Ancillary, & CTS) valuation differentials under the current 25 bps MSF model.

Illustrative Summary Loan Value Differences:	
<b>Lender A Loan Value</b>	<b>101.91</b>
<i>less Gfees &amp; BU/BD differential impact</i>	<i>(0.14)</i>
<i>less Float &amp; Ancillary differential impact</i>	<i>-</i>
<i>less Cost to Service differential impact</i>	<i>(0.08)</i>
	<b>(0.70)</b>
<i>less Base MSF multiple differential impact</i>	<i>(0.53)</i>
<i>less Excess IO multiple differential impact</i>	<i>(0.09)</i>
<i>less Net Cost to Originate differential impact</i>	<i>-</i>
<b>Lender B Loan Value</b>	<b>101.08</b>

Loan Assumptions	
Loan Amount (\$)	\$175,000
Expected Duration/WAL (yrs)	5.00
<b>Base MSF (bps)</b>	<b>25.00</b>
MBS Coupon Price (bps)	101.00
Excess Spread contractually part of MSR	TRUE

	Lender A <i>(price setter)</i>	Lender B <i>(price taker)</i>
Mortgage banking spread (bps) <i>(priced by lender at origination)</i>	<b>40.0</b>	
Excess Spread (bps)	15.0	
Loan Note Rate [=MBS 4% + Gfee + (MSF+XS-IO)]	4.625%	4.625%
Gfee (annual bps)	22.5	26.5
Buy Down multiple	3.4 x	3.4 x
Float & Ancillary NPV (bps)	0.33	0.33
CTS (\$/loan/month)	\$5	\$8
CTS NPV (bps)	13.7	21.9
Base MSF multiple	4.0 x	1.9 x
Excess IO multiple	4.0 x	3.4 x