Loan Costs Channel Study 2024

Prepared by Polygon Research
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Executive Summary

Introduction
United Wholesale Mortgage and Willow Canyon Advisors asked Polygon Research to analyze mortgage lending outcomes from the past 4-6 years having to do with loan costs by loan type, and by Census tract characteristics.

The resulting 2024 Channel Study is a comprehensive investigation of TPO-originated loans in comparison to Retail-originated loans. The goals of the study are to:

1. Compare consumer costs of TPO loans versus retail loans
2. Compare origination statistics in Majority Minority Census Tracts (MMCT) by channel

Our scope is limited to clearly defined origination channels. All of our analysis is based on loan-level data.

Data Sources
The core data sources chosen for the study are the most comprehensive data sets on mortgage lending where channel is defined: the annual Home Mortgage Disclosure Act (HMDA) and the monthly agency single family performance and MBS data sets, staged at the microdata level, comprising over 5 billion detailed loan records, and current with the latest data available as of March/August 2024, depending on the data set.

We leveraged the public HMDA LAR data because it has data on consumer costs, because it is open and because it supports transparency of assumptions and data provenance. We blend HMDA data with Census data curated and published by the FFIEC to provide population patterns in the context of mortgage finance activity.

In the HMDA data we can precisely differentiate among four origination channels (broker, retail, non-delegated correspondent, and delegated correspondent), while in the agency data we only have a clear origination signal only on broker and retail, since from the secondary market perspective, correspondent represents multiple origination channels.

Our cost analysis consisted of 2 primary methods, the first is to compare 2 values: what we call Net Charges and Credits, and Interest Rate. The second is to compare our estimated APR and measurements that derive from APR. The former is based on HMDA alone, while the latter relies on an intensive data matching effort between HMDA data and secondary market data to obtain elements missing from HMDA that drive our estimate of APR. The secondary market data is comprised of the Fannie Mae, Freddie Mac, and Ginnie Mae (the agencies) monthly single-family loan-level credit performance disclosure data sets. These data sets span, as of the date of our publication, from January 2000 to March 2024 for the GSEs, and April 2015 through July 2024 for Ginnie Mae. We restricted our GSE analysis to their primary/standard data - we did not include HARP loans or the non-standard/exclusion data that is not kept current by the GSEs. This scoping provides a large subset of Fannie/Freddie 30-year and less, fully amortizing, full documentation, single-family, conventional fixed-rate mortgages.

Executive Summary (contd.)

Data Scoping and Filter selection
As the outset of our analysis, we took a global view of the market (no filters) and measured overall size and channel market share. We then focused largely on the non-depository lender segment as it is the segment with the largest market share by far, and the one with the common denominator of characteristics such as relying on access to the secondary and having a more broad reach (avoiding localized depository characteristics and fields of membership).

Beyond this, some of our segmentation or filtering followed the through line between our data sets, as discussed above – i.e. “standard” loans sold to the agencies. In each section of our analysis, we clearly disclose the filters we’ve applied.

We discuss the selection of metrics in detail in the study. Because of the coarse-grain nature of the Total Loan Costs field in the public HMDA LAR data, we acknowledge an important constraint – we cannot determine to what extent lenders were responsible for certain discrete components of total loan costs across CD boxes A, B, and C, which include fees like title insurance (e.g. lender and borrower’s title insurance policy and premiums) – and therefore we do not focus total loan costs for our cost comparison. (We do however, include this analysis in the appendix for context). Instead, we focus on the Box A centric HMDA field Origination Charges, and related fields, in building our Net Charges and Credits.

For more details on total loan costs, please see Polygon Research recent response to CFPB’s RFI on Loan Costs.

Executive Summary (contd.)

For the **cost analysis (Objective 1), with our method #1** (HMDA data only), as just discussed, we used the HMDA metrics most salient to the perspective of consumer choice: Box A fees, interest rate, lender credits, and loan amount.

With this scoping, and filters that align with the scope of the GSE performance data noted above, TPO overall performed better than retail, most notably on fees.

In 2023, a year of generation-high interest rates, Home Purchase consumers in the Independent TPO channel paid on average 115 bps upfront to obtain 6.58% average interest rate compared to average 148 bps upfront and 6.60% average interest rate in the Independent Retail channel.

This translates into overall savings of $3,500 per loan or a total of $1.3 Billion savings on all Independent TPO loans in 2023 (assuming all things equal for a loan size of $400,000). Using this loan size, we calculated channel costs for each of the last five years. With the exception of 2020, the Independent TPO channel came out ahead in each year, with savings as high as $12,000 per loan in 2021.

Lifetime loan cost analysis on the average sized loan shows savings for the Independent TPO channel for all three of the loan types, with the largest savings in VA loans.

For refinance loans, consumers in the Independent TPO channel paid higher interest rates but still lower upfront costs than consumers in the retail channel in 2023.

We applied an algorithm to estimate the annual percentage rates (APR) and the total interest percentage (TIP) and used these metrics in our comparisons between channels. These metrics are disclosed to the borrower on the CD and are suitable comparison metric for consumer cost between the channels.

Not only did consumers achieve lower APRs for home purchase loans in the Independent TPO channel in 2023, but looking at the trend since 2020, we observe similar pattern of lower APR in the Independent TPO channel, irrespective of the interest rate environment.

In 2023, the Independent TPO channel estimated APR was 7.00% for home purchase agency loans (complete filters described in the body of the study) while the Independent Retail channel's estimated APR was 7.11% in the same loan segment.

The **cost analysis (Objective 1), with our method #2** (estimated APR) - we calculated 2023 that for a standard loan profile consumer savings of $10,662 over the life of the loan in the Independent TPO channel vs. the Independent Retail channel. Savings for 2020-2022 – also favorable for the TPO channel – are contained in the body of the study.

Executive Summary (contd.)

•Finally, the **analysis of lending in majority-minority Census tracts (Objective 2)** provides summary statistics for lending within MMCT, as well as detailed comparisons between the TPO and retail channels.

•Of the roughly 85,000 census tracts, 29,918, were MMCT, about 35% of all tracts.

•There are 120 million people who live in MMCT or 36% of the U.S. population. But less than 25% of all loan originations happen in MMCTs.

•Borrowers in MMCTs have lower incomes and lower credit scores, and often need loans with low downpayment. Serving the credit needs of borrowers in MMCT has been a priority of all lenders, in all channels, and regulators.

•Analyzing 2023 HMDA LAR data, we see that the Retail channel is the dominant channel serving the credit needs of these borrowers. However, looking at the trend from 2018 through 2023, we observed that increasingly borrowers in MMCT areas are choosing the TPO channel.

•In 2023, more than 1.4 million home purchase agency loans were originated in MMCT. Analyzing the home purchase agency loan segment, there is a direct relationship between minority percentage of Census tracts and TPO market share. For example, the TPO market share increases to 42.3% of agency home purchase originations (1-4 units, closed-end) in 90-100% MMCT compared to 27.2% share in <50% census tracts. On the other hand, there is an inverse relationship between minority percentage of Census tracts and retail market share.

•The Independent TPO channel has higher approval rates (for all loans) in MMCT ~70% vs. 58% for Independent Retail, as well as non-MMCT ~75% vs. 64% for Independent Retail. This has helped both borrowers in MMCT access housing finance as well as the Independent TPO lenders to gain more market share, and in some cases to take market share of incumbents such as depositories, or other established retail lenders.

•Although geographic analysis is beyond the scope of the present study, we included a few analyses in the Appendix to understand the role of Independent TPO in MMCT. We focused first on the top 10 metro areas by number of people living in MMCTs, and then in rural areas. Our analysis showed that in these top 10 urban areas, Independent Retail continues to play a significant role in providing mortgage finance, but its market share has slowly decreased from 37.9% in 2018 to 35.7% in 2023. Conversely, the market share of Independent TPO has steadily increased from 16.7% in 2018 to 23.2% in 2023.

•We used “Not in Defined MSA” as a proxy for rural areas. A very small portion of the loans were originated to borrowers in MMCTs in rural areas – slightly more than 50,000 loans, or 7.25% of loans originated in rural areas. The top states for rural MMCT originations are Texas, North Carolina and Mississippi (in the South region), and in the West region the top states are New Mexico, Hawaii, and Colorado (West region). The Independent TPO channel had a smaller market share of 9.7% in 2023, but this was up from 7.2% in 2018.

Executive Summary (contd.)

The high percentage of home purchase loans originated to minority borrowers through the broker channel suggests that this channel plays a crucial role in promoting homeownership among underserved communities. Brokers are more successful than retail loan officers in serving minority borrowers because mortgage brokers often have local presence and can better understand the unique needs of their communities, including minority borrowers. Additionally, brokers have access to a wide range of loan products from multiple lenders, allowing them to find solutions that fit the specific financial situations of minority borrowers. Brokers are also in a better position to provide one-on-one guidance and support throughout the mortgage process, helping minority borrowers navigate the complexities of homebuying. Some brokers have established relationships with community organizations, housing counseling agencies, and real estate professionals who work closely with minority communities.

VA borrowers who obtained their loans through the wholesale channel received a 6.26% rate on average compared to a 6.40% rate from retail lenders and had to pay less than a percentage point (87bps on the loan amount) compared to the retail channel (106bps).

Putting the two main objectives together, namely consumer costs and savings by channel and serving MMCT areas by channel, our analysis points to the following takeaways:

Over the life of the loan, consumers save in the Independent TPO channel. Using an estimated 2023 APR for 30YR FRM Home Purchase Agency Loan and a standard loan profile, we calculated that consumers save $10,662 over the life of the loan compared to Independent Retail channel. Strictly using native HMDA data, the TPO showed savings as well, a notable example being a lifetime of the loan savings of $13,432 for VA loans.

While the TPO Channel is not the dominant channel for mortgage finance in MMCT areas, it has been increasing its presence in MMCT. The Independent TPO market share, based on all originations, has increased in top urban MMCT areas to 23.2% eclipsing the Bank Retail channel.