Ginnie Mae
Our Guaranty Matters

GLOBAL MARKETS ANALYSIS REPORT

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Table of Contents

Inside this Month's Global Market Analysis Report... 1
Highlights 2
1 US Aggregate and Global Indices 5
1.1 Bloomberg US Aggregate and Global Indices 5
2 Sovereign Debt Product Performance Comparisons 6
2.1 Global 10-Year Treasury Yields (Unhedged) 6
2.2 US Treasury Hedged Yields 7
SECONDARY MORTGAGE MARKET 8
3 Fixed Income Product Performance Comparisons 8
3.1 Ginnie Mae Yields – USD 8
3.2 Ginnie Mae Hedged Yields 9
3.3 Ginnie Mae Yield Spreads – Intermediate Credit 10
3.4 Global Treasury Yield Per Duration 11
4 Prepayments 12
4.1 Aggregate Prepayments (CPR) 12
4.2 Involuntary Prepayments (CDR) 13
4.3 Voluntary Prepayment Rates (CRR) 14
5 Single-Family MBS Pass-Through Issuance 15
5.1 Gross Issuance of Agency MBS 15
5.2 Net Issuance of Agency MBS 17
5.3 Monthly Issuance Breakdown 19
5.4 Percent Refi at Issuance – Single-Family 20
6 Agency Single-Family MBS Outstanding 21
6.1 Outstanding Single-Family Agency MBS 21
6.2 Origination Volume and Share Over Time 22
6.3 Agency Issuance and Agency Outstanding by State 23
6.4 Outstanding Ginnie Mae MBS Volume by Coupon and Vintage Over Time 24
7 Agency REMIC Securities 25
7.1 Monthly REMIC Demand for Ginnie Mae MBS 25
7.2 REMIC Market Snapshot 26
8 MBS Ownership 27
8.1 Commercial Bank Holdings of Agency MBS 27
8.2 Bank and Thrift Residential MBS Holdings 28
8.3 SOMA Holdings 30

8.4 Foreign Ownership of MBS 31
8.5 Foreign Ownership of Agency Debt and Agency MBS 32
9 Fixed Income Liquidity Indicators 33
PRIMARY MORTGAGE MARKET 34
10 Agency Credit Breakdown 34
10.1 Credit Scores 34
10.2 Loan-to-Value (LTV) 36
10.3 Debt-to-Income (DTI) 38
10.4 High LTV Loans: Ginnie Mae vs. GSEs 40
10.5 Serious Delinquency Rates 41
10.6 Credit Box 42
10.7 Credit Box: Historical 44
11 Forbearance Trends 46
12 Holders of Ginnie Mae Mortgage Servicing Rights 47
13 Agency Nonbank Originator 48
13.1 Bank vs. Nonbank Originators Historical Credit Box, Ginnie Mae vs. GSE....50
13.1.1 (FICO, LTV, DTI) 50
14 Environmental, Social, and Governance 54
14.1 Environmental, Social, and Governance: A Summary 54
14.2 Environmental 55
14.3 Social 55
14.3.1 Low-to-Moderate Income Borrowers 56
14.3.2 Purchase and Refinance Origination by Income Bracket 57
U.S. HOUSING MARKET 58
15 Housing Affordability 58
15.1 Housing Affordability – Home Price Appreciation 58
15.2 Housing Affordability – Inflation, Wages, and the Price of Real Estate 59
15.2.1 Housing Affordability – Mortgage Rate Trends 61
15.3 Housing Inventory 62
15.4 Size and Value of the US Housing Market 63
16 Disclosure 64

Inside this Month's Global Market Analysis Report...

This month's *Highlights* section focuses on perspectives from market participants in East Asia regarding Ginnie Mae MBS and the broader Agency MBS market. The *Highlights* provide investment community perspectives on Agency MBS in the three largest markets for Ginnie Mae MBS outside of the United States: China, Japan, and Taiwan. It captures current trends as well as future concerns of East Asian investors as it relates to the Ginnie Mae MBS market.

Notable insights in this month's Global Market Analysis Report include the following:

- The Fixed Income Product Performance Comparisons section shows that Ginnie Mae MBS continue to offer attractive yields relative to sovereigns with comparable durations globally.
- The Single-Family MBS Pass-Through Issuance section captures the dominant role government lending/mortgage insurance programs are playing in the mortgage market post-pandemic. Gross and net issuance of single-family Ginnie Mae pass-throughs exceeds that of both Fannie and Freddie Mac.
- The Environmental, Social, and Governance section takes note of the newly introduced Ginnie Mae Social Bond program, announced by President Alanna McCargo.
- The U.S. Housing Market section illustrates the recent cool down in home price appreciation. The section also captures the fact that affordability remains a significant issue driving overall MBS issuance down.

Highlights

For the *Global Market Analysis Report's* September 2023 publication, a series of questions were posed to fixed income market participants in East Asia that trade securitized products, including Agency MBS. The focus was on China, Japan, and Taiwan, given that they are the three largest foreign holders of Agency MBS. The responses have been edited for readability.

1. In terms of financial institution types, what does the institutional investor landscape look like in East Asia with regard to investment in Ginnie Mae MBS?

Typically, three types of investors historically buy GNMA MBS in Asia: banks, insurance companies, and in some cases, asset managers. In 2023, the majority of East Asian MBS investors are banks, rather than insurance companies. In China, most banks see MBS as an alternative to investment grade corporate bonds when the mortgage basis is wide. Also, we have seen some securities firms trading both MBS pools and TBAs as a short-term directional trade. In Japan, banks are mainly interested in CMO floaters and MBS pools, which are typically financed through repo. There are insurance companies and money managers interested in MBS pools and TBA as well. In Taiwan, like other areas, banks rather than insurance companies are the main MBS audience, and they are interested in both CMOs (short Sequential Play Classes, Planned Amortization Classes or floaters) and pools. There are some duration needs from insurance companies and money managers in Taiwan, but their transaction volume is lower than in prior years. Finally, some central banks in East Asia are active in the MBS market as well.

Asian central banks have typically had a very close alignment with the USD and connection with the Fed as the dollar has been, for many decades, the only reserve currency of choice with both global liquidity and the depth of asset classes to satisfy growing central bank reserve accumulation. Asian central banks, in a number of cases over recent history, had a peg to the USD due to volatility in their own domestic markets, hence the dollar has been a valuable reserve tool to protect domestic currencies. As Asian central banks have become accustomed to the dollar, and with reserves in USD usually comprising around 50 percent of their entire reserves, the need to diversify with high quality assets has been important, especially as reserves have grown substantially away from US Treasury securities. Diversification has supported adding Ginnie Mae products, which offers an explicit government guaranty but with the added dimension of a spread in excess of Treasury security yields. In addition, since the financial crisis, Ginnie Mae stands out as the bellwether for the mortgage market due to its depth of liquidity and explicit guaranty. All these factors highlight the safety and importance of this asset class for reserve investments but with the added benefit of incremental yield over government debt and even sovereign/supranational debt.

2. Do East Asian investors view Ginnie Mae MBS as a highly liquid financial instrument? If so, what considerations contribute to this view?

Investors regard Ginnie Mae MBS pools and TBAs as highly liquid financial instruments. The full faith and credit US government guarantee and scalability on trades are key: USD 100 million-plus transaction size is common on current coupon trades with a tight market.

3. **What value do East Asian institutional investors place on the explicit full faith and credit guaranty of the US government on Ginnie Mae MBS?**

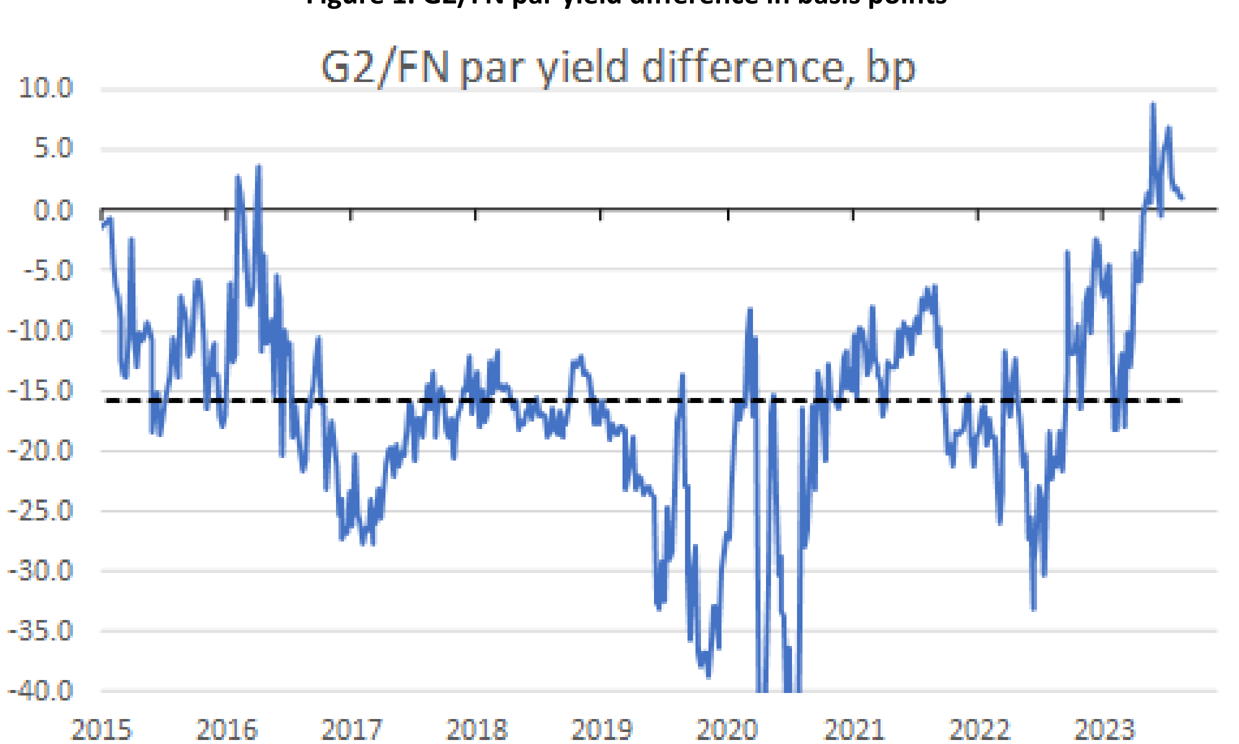
The full faith and credit guaranty of the US government on Ginnie Mae MBS is very important. In general, many investors in Asia consider Ginnie Mae a zero risk-rating and Level 1 asset under Basel III. In fact, for some East Asia broker/dealers, 80-90% of mortgage-backed security trades currently, in both CMO and passthrough, are Ginnie Mae securities. Many Asia clients invest in Ginnie Mae MBS because of the explicit guarantee. In comparison, the implicit guarantee from UMBS has so far generated less demand. This difference is very relevant for bank treasuries in particular, as they need to meet liquidity ratios by owning high quality liquid assets (HQLA). Having said that, certain jurisdictions may need further clarification with local regulators on Ginnie Mae vs UMBS HQLA treatment.

4. **What are the factors that drive relative value of Ginnie Mae MBS and REMIC products for East Asian mortgage securities investors?**

The size and liquidity, the explicit guarantee by US government and the flexible structuring capability in REMICs drive relative value of Ginnie Mae MBS and REMIC products. Also, relative value versus Asian credits is a key factor for relative value considerations in China.

The graph below demonstrates the relative attractiveness of Ginnie Mae MBS compared to conventional MBS on a historical basis.

Figure 1. G2/FN par yield difference in basis points



5. What looks attractive in the Ginnie Mae MBS coupon stack from the perspective of East Asian Ginnie Mae MBS institutional investors?

Most Asia investors like current coupon MBS priced at par or slightly below. Currently, the current coupon GNMA MBS is 6% (G2SF 6) and it offers an attractive yield, and the dollar price is at a discount, thus having less exposure to premium/prepayment risk. Asian investors prefer to buy MBS current coupons given that there is no clear view at this point in time regarding interest rate direction and future Fed action. Lower coupon MBS have a lower yield relative to the hedge and funding costs, and both factors are not favorable for Asia investors.

6. Is there anything else that is top of mind for institutional investors in East Asia about Ginnie Mae MBS?

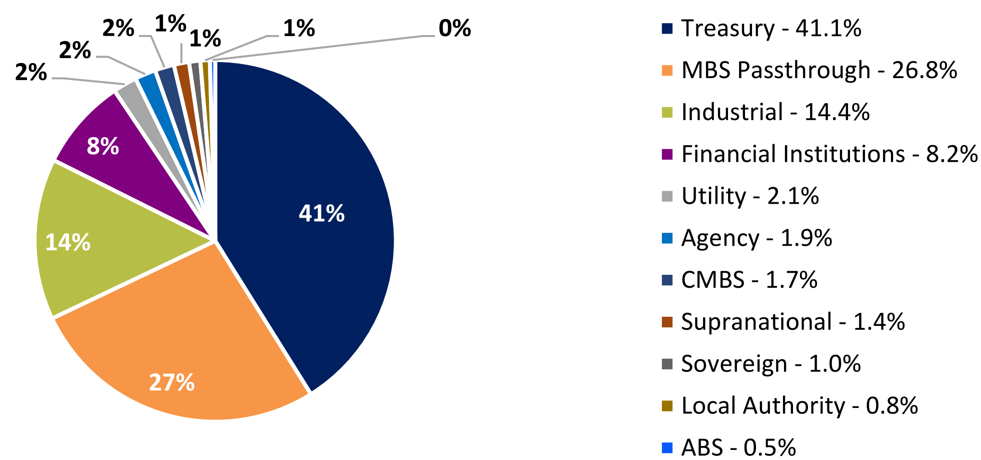
While many investors agree that MBS spreads are attractive, they are concerned about MBS market technicals in the near future, as banks in North America are currently not as active with MBS purchases. North American banks are historically the largest investors in MBS. Lack of demand from domestic banks leads to attractive MBS yields for investors, but also gives investors concern about the performance of MBS investments in the near term.

1 US AGGREGATE AND GLOBAL INDICES

1.1 Bloomberg US Aggregate and Global Indices

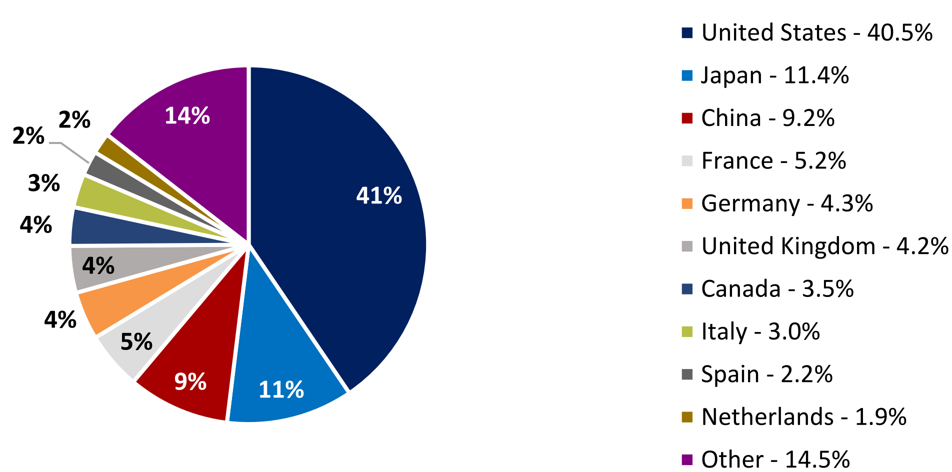
At month-end August, US Treasuries contributed 41.1% to the Bloomberg US Aggregate Index, stable from the prior month. US MBS (Ginnie Mae, Fannie Mae, and Freddie Mac) contributed 26.8%, down approximately 0.1% from the month prior. For the US Aggregate Index, all other changes to the index components were no larger than 1%.

Figure 2. Bloomberg US Aggregate Index



In the Bloomberg Global Aggregate Index by Country, the US share of fixed income remained the largest share of total outstanding issuance, representing 40.5% of the total Bloomberg Global Aggregate Index, flat from the prior month. Japan's share of fixed income was the second highest at 11.4%, down slightly for the third consecutive month. For the Global Aggregate Index, all countries remained stable compared to the prior month with no changes larger than 1%.

Figure 3. Bloomberg Global Aggregate Index by Country



Source: Bloomberg [both charts]. Note: Data as of August 2023. Figures in charts may not add to 100% due to rounding.