

Capital Markets Update

Mark V. Thorpe

Charles C. Williams, CFA

Capital vs. Leverage

- Everyday We All Deal With Regulatory Capital Ratios vs. Gains From Financial Leverage
- We Want More Capital – You Want To Put Up Less
- The Once Comfortable Capital Markets Are Struggling To Find A New Balance Point

Capital vs. Leverage

Why Are Mortgage Products Priced Like This?

- Higher Perceived Risk → Higher Returns
- De-leveraging → More Capital
- Greater Distrust Among Counterparties



RESEARCH

Financial Institutions: Mortgage Companies

Important disclosures can be found at the end of this report.

March 7, 2008 Industry Update

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Mortgage Market Overview: It Is All About De-Leveraging!

Summary and Recommendation

- De-leveraging in financial markets continues to wreak havoc, not only on the pricing of non-agency securities, but now also on agency securities. In August 2007, during the first leg of the de-leveraging, FBR estimated that either the system had to attract \$150 to \$250 billion of permanent capital, or the pricing of mortgage assets would adjust downward, which appeared to be the more likely outcome. Today, we estimate the financial industry needs \$1 trillion of permanent capital to maintain current pricing, which it will be unable to obtain. Without additional capital, prices will fall to levels where the buyers can earn a 15% rate of return. This de-leveraging phenomenon is the main driver of non-agency AAAs trading down to the mid 70s, and agency spreads widening out to a 23-year high. As we wrote back in August 2007, price adjustment will be painful, with many existing portfolios and mortgage originators either failing or becoming much smaller. Already, the adjustment has eliminated most non-agency structured finance companies. We believe that it will take about six to 12 months for the pricing pressure to alleviate on these mortgage assets. There is no quick fix here; it will take time, but will create plenty of opportunities for those financial entities that can take advantage of the current pricing environment.

Mortgage Price Distress

- Global Investors Have Lost Confidence In Mortgage Collateral
- Agency Spreads To UST Near All-time Highs Generating ROEs In 15% Range
- The Capital Markets Are De-leveraging Mortgage Investments

Mortgage Price Distress

- AAA Agency Mortgage Security Carry Trades Require Real Capital; Not Just 20% Risk Based Capital
- Super Senior AAA Tranches Of Mortgage Securitizations Are No Longer Viewed As Risk Free
- AAA Rated SIVs Are No Longer Viewed As Riskless

Mortgage Price Distress

- Non-agency Mortgage Products Are No Longer Viewed As “Almost Agency” Risks
- Non-agency To Agency Spreads Have Increased
- Deleveraging Greater For Non-agency Mortgage Products

Mortgage Price Distress

- Non-agencies Require Even Higher Returns To Attract Investment
- More Capital & Higher Returns → Prices Must Decline!
- For the Riskier Mortgages, The Decline Is Even More Dramatic!

Mortgage Price Distress

- Compared To Agency Prices Of 98 to 101
- Would You Require 10% to 22% ALLLs?
- Non-agency Pricing Appears To Be Based On FEAR, Not Fundamentals

<HELP> for explanation, <MENU> for similar functions.
 Enter 2<go> - 8<go> for loan level details

Mtge **CLP**

Group **All Collateral** **Table** 1) **Expand All** CWALT 2006-17T1 Collateral Performance

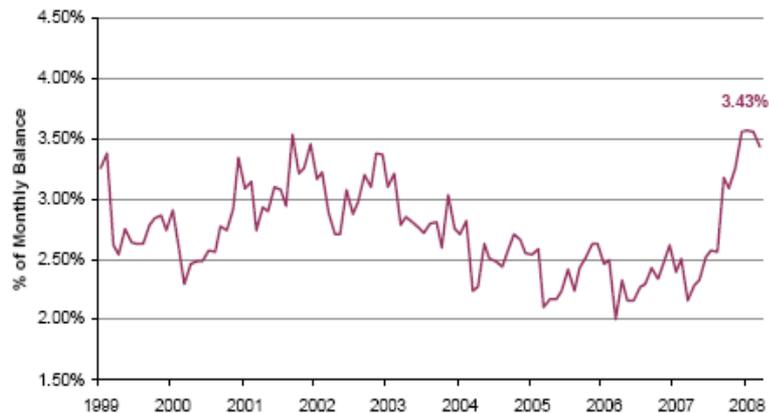
	05/2008	04/2008	03/2008	02/2008	01/2008	12/2007	11/2007	10/2007
USD Bal w/ghtd								
Balance (H)	361,041	365,683	367,670	369,824	374,174	375,508	380,100	382,475
Pool Factor	0.752	0.762	0.766	0.770	0.780	0.782	0.792	0.797
# of Loans	562	567	571	573	579	580	584	586
WAC	6.731	6.729	6.730	6.730	6.728	6.728	6.730	6.731
WAM/Age	331/ 25	332/ 24	333/ 23	335/ 22	336/ 21	338/ 20	339/ 19	340/ 18
WALTV (Amort)	72.57%	72.61%	72.66%	72.83%	72.85%	72.96%	72.98%	72.98%
2) Delinq 30 days	4.30%	3.75%	2.93%	3.13%	4.54%	4.10%	3.17%	2.82%
3) Delinq 60 days	2.60%	1.21%	1.54%	1.77%	0.93%	1.80%	1.44%	2.57%
4) Delinq 90 days	2.95%	4.22%	3.79%	3.48%	4.37%	3.68%	3.39%	1.62%
Bankruptcy	-	-	-	-	-	-	-	-
5) Foreclosure	6.41%	5.00%	4.90%	4.50%	3.42%	2.92%	2.46%	2.75%
6) REO	1.87%	1.67%	1.78%	1.46%	1.35%	1.22%	1.18%	0.86%
7) Delinq. 60+	13.83%	12.10%	12.01%	11.21%	10.07%	9.62%	8.47%	7.80%
8) Delinq. 90+	11.23%	10.89%	10.47%	9.44%	9.14%	7.82%	7.03%	5.23%
Cum. Loss	0.225%	0.176%	0.142%	0.139%	0.131%	0.131%	0.121%	0.122%
Full Document.	28.46%	28.39%	28.36%	28.34%	28.24%	28.32%	28.01%	28.27%
Arm Collat. %	0.00	-	-	-	-	-	-	-
Credit Score	704	704	704	704	704	704	705	705
Balance < 417	4.94	-	-	-	-	-	-	-
1 Mo. CPR	13.50	5.60	6.00	12.40	3.50	12.90	6.50	0.40

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CUSIP #02146AAB4 - 3/31/08 @ 78.1

**NATIONAL DELINQUENCY RATES: PRIME, ALT-A & SUBPRIME LOANS
(CHART 10)**

**Prime: 30, 60 & 90+ Days Delinquent
1999 - March 2008**



(CHART 11)

**Alt A: 30, 60 & 90+ Days Delinquent
1999 - March 2008**



(CHART 12)

**Subprime: 30, 60 & 90+ Days Delinquent
1999 - March 2008**



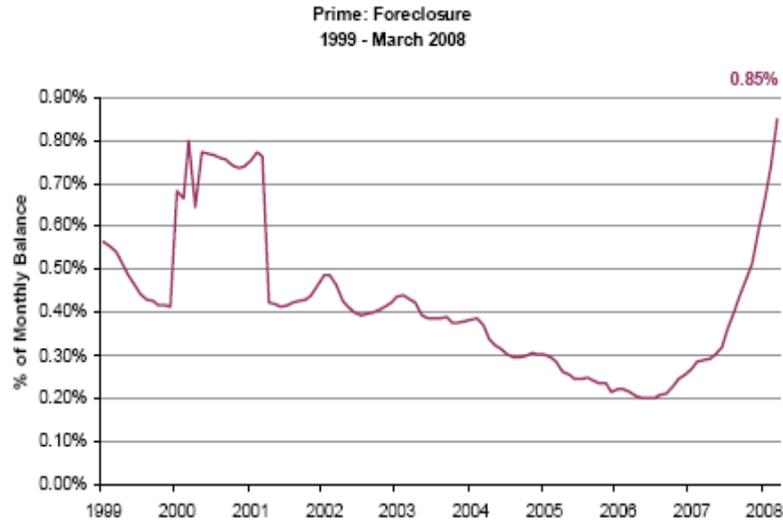
SOURCE: CHARTS 5-15 LOAN PERFORMANCE, A SUBSIDIARY OF FIRST AMERICAN REAL ESTATE SOLUTIONS

NOTE: DATA USES ACTIVE LOAN DOLLAR BALANCES ON A MONTHLY BASIS; ALT A IS DEFINED AS ORIGINAL CREDIT SCORE 620-659 AND LTV AT ORIGINATION > 80%.

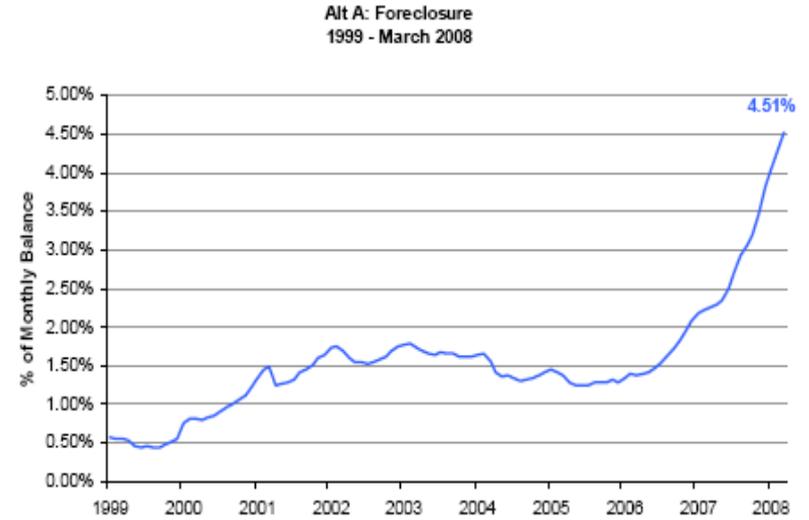
ALL VARIATIONS OF DOCUMENTATION ARE INCLUDED. DATA FOLLOWS THE MBA DEFINITION OF DELINQUENCY.

OTS MMM #0508 6/5/2008

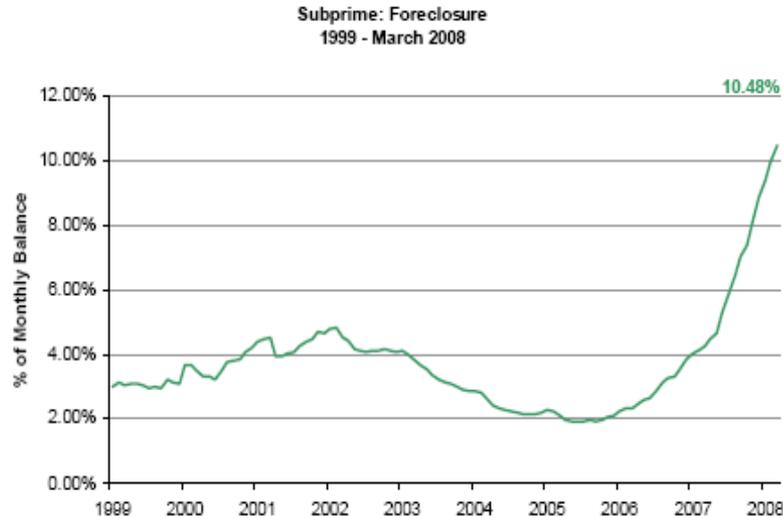
NATIONAL FORECLOSURE RATES: PRIME, ALT-A & SUBPRIME LOANS
(CHART 13)



(CHART 14)



(CHART 15)



SOURCE: CHARTS 5-15 LOANPERFORMANCE, A SUBSIDIARY OF FIRST AMERICAN REAL ESTATE SOLUTIONS

NOTE: DATA USES ACTIVE LOAN DOLLAR BALANCES ON A MONTHLY BASIS; ALT A IS DEFINED AS ORIGINAL CREDIT SCORE 620-659 AND LTV AT ORIGINATION > 80%.

ALL VARIATIONS OF DOCUMENTATION ARE INCLUDED. DATA FOLLOWS THE MBA DEFINITION OF DELINQUENCY.

OTS MMM #0508 6/5/2008

<HELP> for explanation, <MENU> for similar functions.
 Enter 2<go> - 7<go> for loan level details

Mtge **CLP**

Group **All Collateral** **Table** 1) **Expand All** CWALT 2003-15T2 Collateral Performance

	05/2008	04/2008	03/2008	02/2008	01/2008	12/2007	11/2007	10/2007
USD Bal Wgtd								
Balance (H)	58,386	59,257	61,102	61,196	61,669	61,757	63,471	63,559
Pool Factor	0.195	0.198	0.204	0.204	0.206	0.206	0.212	0.212
# of Loans	131	133	136	136	137	137	141	141
WAC	6.279	6.278	6.298	6.298	6.300	6.300	6.313	6.313
WAI/Age	296/ 60	296/ 59	297/ 58	299/ 57	300/ 56	301/ 55	302/ 54	303/ 53
WALTV (Amort)	66.92%	66.58%	66.64%	66.74%	66.87%	66.97%	67.39%	67.48%
2) Delinq 30 days	4.22%	4.47%	1.22%	3.01%	3.31%	3.59%	0.58%	1.47%
3) Delinq 60 days	1.20%	0.62%	2.02%	2.57%	2.60%	2.00%	1.95%	1.95%
4) Delinq 90 days	5.30%	5.31%	4.30%	4.34%	3.71%	3.71%	4.01%	3.12%
Bankruptcy	-	-	-	-	-	-	-	-
5) Foreclosure	1.15%	1.13%	0.54%	1.46%	2.98%	2.98%	2.52%	3.05%
REC	0.00%	0.00%	1.55%	1.55%	0.00%	0.00%	0.00%	0.00%
6) Delinq. 60+	7.65%	7.06%	8.41%	9.92%	9.29%	8.69%	8.48%	8.12%
7) Delinq. 90+	6.45%	6.44%	6.39%	7.35%	6.69%	6.69%	6.53%	6.17%
Cum. Loss	0.342%	0.342%	0.173%	0.173%	0.173%	0.173%	0.173%	0.173%
Full Document.	21.84%	21.55%	20.92%	20.92%	20.79%	20.79%	20.84%	20.84%
Arm Collat. %	0.00	-	-	-	-	-	-	-
Credit Score	674	675	675	675	675	675	674	674
Balance < 417	49.52	-	-	-	-	-	-	-
1 Mo. CPR	15.00	29.70	0.30	7.40	0.20	26.90	0.20	0.10

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Mtge **CLP**

Enter 2<go> - 8<go> for loan level details

Group **All Collateral** **Table** 1) **Expand All** CWHL 2003-24 Collateral Performance

	05/2008	04/2008	03/2008	02/2008	01/2008	12/2007	11/2007	10/2007
USD Bal w/ghtd								
Balance (H)	190,936	192,042	193,737	195,593	198,700	200,311	201,731	203,575
Pool Factor	0.382	0.384	0.387	0.391	0.397	0.401	0.403	0.407
# of Loans	449	452	455	459	466	469	472	476
WAC	5.892	5.893	5.894	5.894	5.894	5.895	5.894	5.894
WAI/Age	288/ 60	289/ 59	290/ 58	291/ 57	292/ 56	293/ 55	294/ 54	295/ 53
WALTV (Amort)	63.16%	63.26%	63.36%	63.48%	63.62%	63.68%	63.84%	64.05%
2) Delinq 30 days	0.59%	0.54%	0.99%	0.49%	1.20%	0.48%	0.10%	0.71%
3) Delinq 60 days	0.24%	0.22%	0.00%	0.24%	0.00%	0.00%	0.21%	0.00%
4) Delinq 90 days	0.68%	0.46%	0.46%	0.21%	0.21%	0.21%	0.00%	0.18%
Bankruptcy	-	-	-	-	-	-	-	-
5) Foreclosure	0.39%	0.39%	0.39%	0.38%	0.38%	0.37%	0.37%	0.19%
6) REO	0.18%	0.18%	0.18%	0.18%	0.18%	0.18%	0.18%	0.17%
7) Delinq. 60+	1.49%	1.25%	1.03%	1.01%	0.77%	0.76%	0.76%	0.54%
8) Delinq. 90+	1.25%	1.03%	1.03%	0.77%	0.77%	0.76%	0.55%	0.54%
Cum. Loss	0.102%							
Full Document.	-	-	-	-	-	-	-	-
Arm Collat. %	0.00	-	-	-	-	-	-	-
Credit Score	750	750	750	750	750	750	750	750
Balance < 417	52.30	-	-	-	-	-	-	-
1 Mo. CPR	4.80	8.20	9.00	15.60	7.50	6.40	8.60	0.90

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CUSIP #12669ELF1 – 3/31/08 @ 92.3

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 Enter 2<go> - 9<go> for loan level details

Mtge **CLP**

Group **All Collateral** **Table** 1) **Expand All** BSABS 2004-AC3 Collateral Performance

	05/2008	04/2008	03/2008	02/2008	01/2008	12/2007	11/2007	10/2007
USD Bal w/ght								
Balance (H)	135,142	136,857	138,177	139,724	141,446	142,460	143,529	144,610
Pool Factor	0.345	0.350	0.353	0.357	0.361	0.364	0.367	0.369
# of Loans	844	852	860	870	880	886	895	902
WAC	6.266	6.271	6.272	6.274	6.272	6.273	6.276	6.275
WAI/Age	284/ 50	285/ 49	286/ 48	288/ 47	288/ 46	290/ 45	291/ 44	291/ 43
WALTV (Amort)	68.26%	68.49%	68.64%	68.77%	68.85%	69.00%	69.10%	69.15%
2) Delinq 30 days	1.66%	1.31%	0.64%	1.34%	1.30%	1.13%	0.84%	0.50%
3) Delinq 60 days	0.42%	0.00%	0.07%	0.20%	0.41%	0.31%	0.38%	0.77%
4) Delinq 90 days	0.43%	0.45%	0.44%	0.60%	0.40%	0.34%	0.15%	0.45%
5) Bankruptcy	0.84%	0.81%	1.04%	1.03%	0.97%	0.83%	0.74%	0.89%
6) Foreclosure	1.50%	1.52%	1.49%	1.81%	1.92%	1.66%	1.55%	0.90%
7) REO	1.22%	1.49%	1.48%	1.09%	0.62%	0.73%	0.73%	0.62%
8) Delinq. 60+	3.57%	3.46%	3.48%	3.70%	3.35%	3.04%	2.81%	2.74%
9) Delinq. 90+	3.15%	3.46%	3.41%	3.50%	2.94%	2.73%	2.43%	1.97%
Cum. Loss	-	0.382%	0.358%	0.346%	0.334%	0.310%	0.307%	0.306%
Second Lien	0.00%	0.00%	-	-	-	-	-	-
Full Document.	26.19%	26.01%	26.09%	26.08%	25.97%	26.14%	26.06%	25.91%
Arm Collat. %	0.00	-	-	-	-	-	-	-
Credit Score	701	701	701	701	701	700	700	700
Balance < 417	81.04	-	-	-	-	-	-	-

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CUSIP #073879BM9 – 3/31/08 @ 90.0

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<HELP> for explanation, <MENU> for similar functions.
 Enter 2<go> - 8<go> for loan level details

Mtge **CLP**

Group **All Collateral** **Table** 1) **Expand All** LABS 2003-1 Collateral Performance

	05/2008	04/2008	03/2008	02/2008	01/2008	12/2007	11/2007	10/2007
USD Bal w/gtd								
Balance (H)	177,108	179,390	182,065	182,850	184,094	184,983	186,523	187,058
Pool Factor	0.418	0.423	0.430	0.432	0.435	0.437	0.440	0.442
# of Loans	543	549	557	559	563	567	572	575
WAC	5.951	5.960	5.961	5.963	5.964	5.966	5.966	5.968
WAI/Age	297/ 56	298/ 55	299/ 54	300/ 53	301/ 52	302/ 51	304/ 50	305/ 49
WALTV (Amort)	63.01%	63.24%	63.36%	63.49%	63.63%	63.79%	63.93%	64.06%
2) Delinq 30 days	0.13%	0.35%	0.90%	0.53%	0.81%	1.21%	0.90%	1.21%
3) Delinq 60 days	0.14%	0.39%	0.33%	0.19%	0.12%	0.03%	0.21%	0.51%
4) Delinq 90 days	0.51%	0.30%	0.39%	0.34%	0.23%	0.25%	0.15%	0.11%
Bankruptcy	-	-	-	-	-	-	-	-
5) Foreclosure	0.48%	0.40%	0.15%	0.14%	0.18%	0.09%	0.00%	0.26%
6) REO	0.05%	0.11%	0.11%	0.16%	0.12%	0.12%	0.16%	0.19%
7) Delinq. 60+	1.18%	1.20%	0.98%	0.83%	0.65%	0.49%	0.52%	1.07%
8) Delinq. 90+	1.04%	0.81%	0.65%	0.64%	0.53%	0.46%	0.31%	0.56%
Cum. Loss	0.107%	0.099%	0.100%	0.085%	0.087%	0.087%	0.071%	-
Full Document.	-	-	-	-	-	-	-	-
Arm Collat. %	0.00	-	-	-	-	-	-	-
Credit Score	-	-	-	-	-	-	-	-
Balance < 417	49.66	-	-	-	-	-	-	-
1 Mo. CPR	12.90	15.00	3.50	6.40	4.20	8.10	1.90	2.60

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CUSIP #525170BL9 – 3/31/08 @ 89.4

Mortgage Price Distress

- Substandard? – Most Likely
- OTTI? – Not My Call!
- 9% -12% Losses? – Nowhere Near Yet!
- Are These Prices Irrational?

TED SPREAD

A Measure Of Uncertainty In
Today's Financial Distress

<HELP> for explanation, <MENU> for similar functions.

Index **DEF**

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TED SPREAD

Bloomberg Financial Definition

Ted Spread. The price difference between three-month futures contracts for U.S. Treasuries and three-month contracts for Eurodollars having identical expiration months.

The Ted spread can be used as an indicator of credit risk. This is because U.S. T-bills are considered risk free while the rate associated with the Eurodollar futures is thought to reflect the credit ratings of corporate borrowers. As the Ted spread increases, default risk is considered to be increasing, and investors will have a preference for safe investments. As the spread decreases, the default risk is considered to be decreasing.

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Index DES

At 19:00 Op .83 Hi .83 Lo .83

TEDSP G INDEX

GP - Line Chart

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Range **07/02/07 - 06/03/08** Upper Line Chart How. Avgs

Period **Daily** US0003H Index - US003H Index



Last Price	0.8295
High on 08/20/07	2.1021
Average	1.2538
Low on 07/21/07	0.3569

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July 2007 To Last Week

TED Spread

- TED = 3 Mo. LIBOR vs. 3 Mo. UST
- Historically 25 – 50 BP Range
- Previously 5 BP Swing Very Severe
- Spread More Than 2 X Average
- Peaked At Almost 7 X Average
- Now TED = Measure Of **DIS**trust Of Global Capital Markets Players

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Index DES

At 19:00 Op .83 Hi .83 Lo .83

TEDSP G INDEX

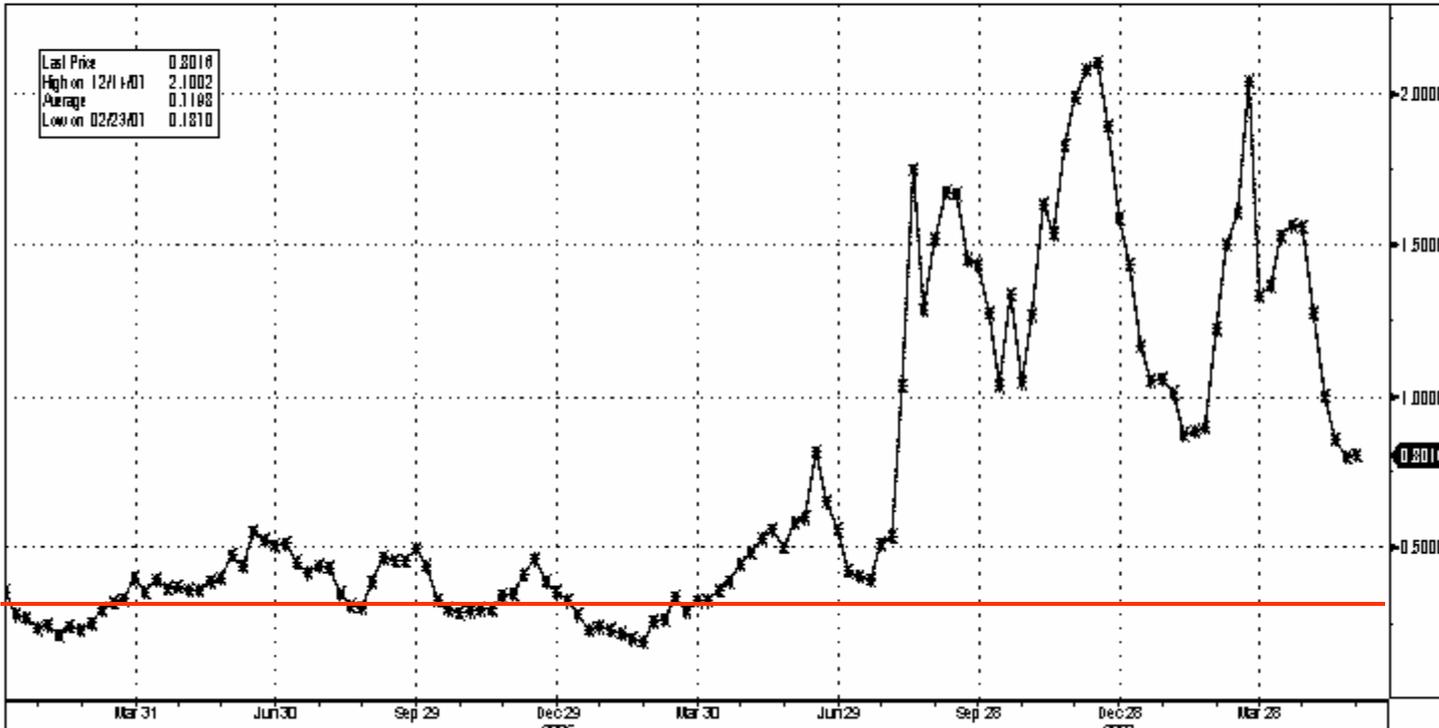
GP - Line Chart

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Range **01/06/06** - **05/30/08** Upper Line Chart How. Avgs

Period **Weekly**

US0003H Index - US0003H Index



35 BP

Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000
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January 2006 Thru May 2008

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Index DES

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TEDSP G INDEX

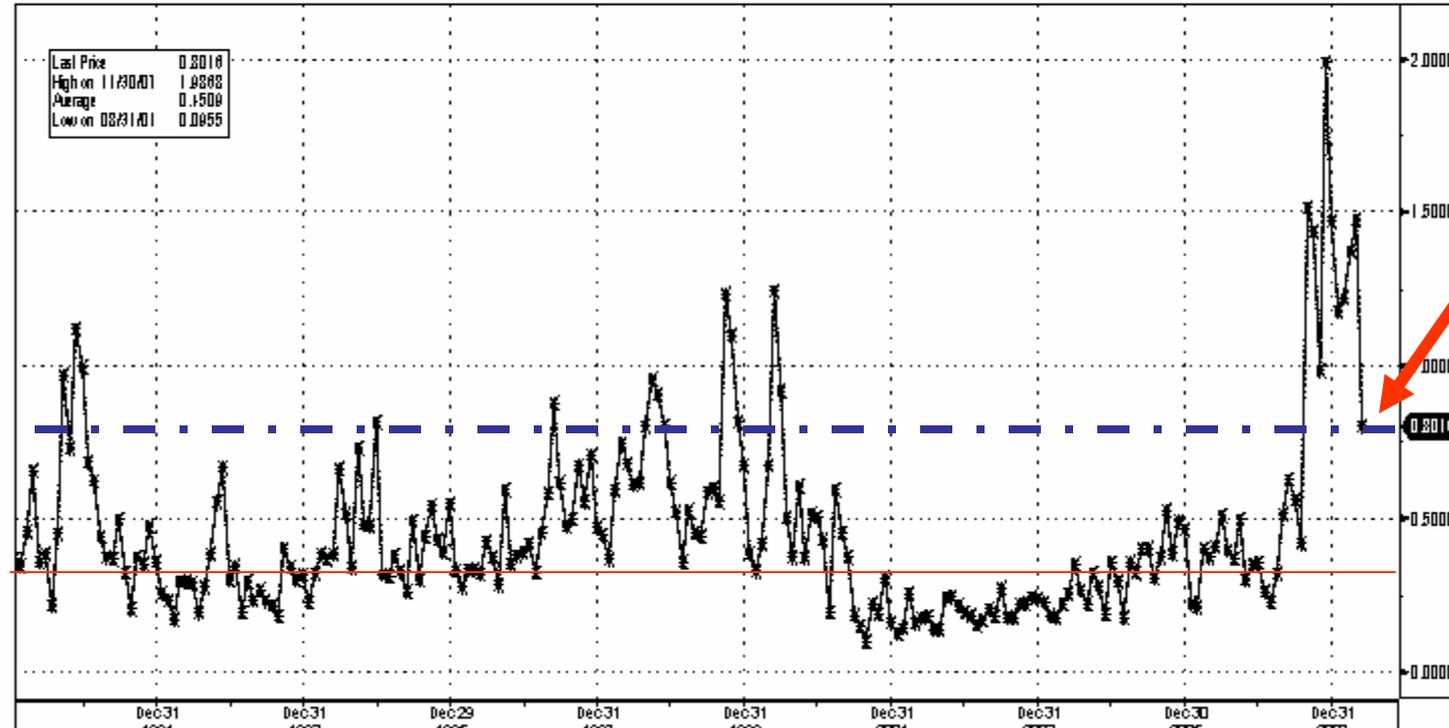
GP - Line Chart

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Range **01/31/90** - **05/30/08** Upper Line Chart How. Avgs

Period **Monthly**

US0003H Index - US0003H Index



82 BP

Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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January 1990 Thru May 2008

Counterparty Risk In The Investment Grade Universe

Investment Grade Counterparty Risk

- Liquidity Constraints
- Risk Based Capital Changes
- Accounting Pains
- Changed Risk Profiles
- “New” Assets To Classify

Investment Grade Counterparty Risk

Liquidity Constraints

- Reduced Wholesale Borrowing Avenues
- Deposit Costs Not Falling In Step With Treasury Interest Rates
- “Long Term Liquidity” Plans Not Working
- Our Presumptions Are Not Aligning With The Market’s Realities

Investment Grade Counterparty Risk

Liquidity Constraints

- For Some, FHLB Only Borrowing Source
- Agency Reverse Repos Uncertain
- Whole Loan RR No Longer Exists
- Brokered CD Rates Much Higher On Greater Demand

Investment Grade Counterparty Risk

Liquidity Constraints

- LRM Will Be A Regulatory Focal Point For The Foreseeable Future
- Not So Simple Any More

Investment Grade Counterparty Risk

Liquidity Risk Management

- TB 77 Remains The Primary Guidance On Best Practices Of LRM
- LRM Article In *Quarterly Review of IRR*
 - Basel W/G On Liquidity
 - US Interagency LRM Guidance

Investment Grade Counterparty Risk

R/B Capital – Mortgage Assets Can Shift To Different Buckets

- Downgraded Non-Agency Mortgage Securities Can Move To 100% Bucket
- RIK Of Downgraded Collateral – Scenarios For All Shifting To R/B Bucket Of Lowest Rated Bond

Investment Grade Counterparty Risk

Unexpected Consequences Of Previous Investment Classification Decisions

- HTM vs. AFS – Coming Home To Roost
- A Material OTTI Charge Can Change Regulatory Capital Position
- Prior HTM To AFS Transfers And OTTI Is Income Charge, Not OCI Adjustment

Investment Grade Counterparty Risk

Changed Risk Profiles

- Previously Safe Muni Bonds Riskier Now
 - Disintegration Of Auction Rate Market
 - Termination Costs Encountered By Issuers To Change Their Funding Structure
- Some AA & AAA Rated Private Label ABS At Substantial Risk Of Loss
- Whole ARM Loan CMOs → Will They Lose Their AAA Ratings?

Investment Grade Counterparty Risk

“New” Assets to Classify

- Many Must Face And Resolve Securitized Asset Classification Issues, Maybe For The First Time
- Securities Are Classified Under Same Guidelines As Loans
- Less Than Fully Realized Contractual Cash Flows Should Be Classified

Sensitivity To Market Risk

Implications Of Current
Marketplace Distresses

Sensitivity To Market Risk

- “New” Market Pricing Is More Volatile!
- What Are Rate Shocked Prices Now?
- Different Credit Spreads Have Moved Prices
 - Is This A New “IRR Sensitivity” Component?
- It Is A “Market Risk” Component!

Sensitivity To Market Risk

Modeling Assumptions That Were
“Generally Accepted” Are Not Working!

- How Do You Estimate Cash Flow Now?
- What Is The Prepayment Rate For A Pool With 20% Highly Delinquent, But 80% Performing As Agreed?
- What LGD Is Right? → But, Then Where Can You Find It?

Sensitivity To Market Risk

- OTS ENPV Model's Mortgage Pricing Mechanism Starts With Quotes On A Huge Universe Of Traded Debt Securities → We Start From PRICES!
- If Your Model Is Cash Flow Driven But Not Adjusted For Market Factors, Or A Level III Process, We WILL Have Differences!
- Document, Document, Document !!!

Mortgage Mutual Funds

Market “Prices” vs. “Reasonable
Valuations”

Schwab vs. Shay

- Schwab's Action Different From Shay's
- Schwab's Liquidations Took NAV To \$7.50
- Maybe Not Institution Oriented?
- Conservative Today, Gains Tomorrow?
- Which Is Right?

Schwab vs. Shay

- Shay Is Protecting Shareholder Value Within The Rules They Can Play By
- Valuation Efforts Are Extensive, No Specific Concerns By Regulators Or FHLB, Yet.
- By Closing Fund To New Investors And Implementing RIK, Avoided Being Forced To Recognize “Last Executed Trade” As Fair Value Of Entire Portfolio.

Shay AMF Conference Call

- I Monitored The June 4 Call To Investors.
- I Will Try To Help Clarify Any Capital Markets Questions You Might Have, If I Can.