THE FUTURE OF THE SECONDARY MORTGAGE MARKET

Has the secondary mortgage market planted the seeds of eventual demise for the traditional mortgage loan system?

by Jack Harris

Since the mid-1970s, the U.S. mortgage market has undergone profound change. Deregulation and volatile interest rates have transformed the mortgage lending industry from a somewhat insular financing area into a more integral component of the larger credit markets. While the changing environment has created difficulties for savings and loan associations, it has provided fertile ground for the growth of a secondary mortgage market. Federally sponsored secondary market agencies (Fannie Mae, Freddie Mac) have been established to assist mortgage lenders in overcoming the inherent problems of making long-term loans with locally derived, short-term funds. Yet some believe the secondary market agencies are encroaching on the viability of depository lending institutions, even implying that they contributed to the irresponsible expansion of the savings and loans, which has lead to the current thrift industry debacle.

Given the uncertain nature of the savings and loan industry at the present time, secondary mortgage markets may play an even stronger role in the provision of housing financing in the future. However, the shape of the secondary mortgage market, and increasingly the entire home mortgage industry, will hinge on several major issues. While it is not possible to foresee the future, it is worthwhile to make educated speculations based on current trends. The following article is one reading of these trends. The article examines the major issues that will help determine the future development of the secondary mortgage market. In the sections that follow, the article addresses these key questions:

- Can the secondary mortgage market continue its extraordinary growth of recent years, or has it reached its peak?

- What is the role of purely private firms in securitizing real estate debt? Will they be crowded out by the federal secondary market agencies?
- What are the prospects for the development of secondary markets for a wider variety of real estate loans? What are the major obstacles to this development?
- What does a strong secondary mortgage market mean for primary mortgage lenders?

Development Of A Secondary Market For Mortgages

In 1988, 44% of the $240 billion of mortgage loans closed by institutions insured by the Federal Savings and Loan Insurance Corporation (FSLIC) were sold into the secondary market; of the loans made for purchase of one- to four-unit dwellings, 61% were sold into the secondary

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market.[1] In addition, virtually all of the $85 billion of loans made by mortgage bankers entered the secondary market. Clearly, a system of home financing that began as a collection of independent institutions formed for gathering deposits locally to make loans has become a system of mortgage lenders that are performing a more specialized task: the origination of loans that eventually will be absorbed into vast securitized pools.

Is Continued Growth Inevitable?

Since the mid-1970s, the secondary mortgage market has grown from an ancillary supplement to the primary market, to a dominant part of the home loan system. Note the rapid increase in the share of mortgages held in mortgage pools, which are portfolios of loans formed in the secondary market as collateral for mortgage-backed securities (Table 1). To some observers, growth of the secondary mortgage market signals an inevitable trend away from traditional avenues of mortgage lending toward full integration of all segments of the capital markets. To others, this past growth has merely been the result of a unique combination of factors that are not likely to be maintained. Therefore, these observers believe, the size and importance of the secondary mortgage market may have already reached a high watermark, and the secondary market may begin to recede from its current level. Which of these views is correct depends on how the other issues discussed in this article are resolved.

Deregulation

There is no question that the recent growth of the secondary mortgage market is the result of a combination of economic, technological and institutional developments, most of which have undermined the viability of traditional, deposit-taking institutions and the institutions' ability to satisfy the demand for housing credit. Possibly the most important of these developments, however, have been the deregulation of home financing institutions and the economic conditions that made deregulation inevitable. On first examination, this may seem an odd statement. One of the reasons the secondary mortgage market exists is to overcome the problems of lenders subject to deposit yield ceilings.

In the past, regulated deposit rate limits prevented savings associations from competing for funds when short-term interest rates rose, and the resulting disintermediation forced a moratorium on new lending activity. The secondary mortgage market, by tapping credit markets directly, supplied the necessary liquidity for new loans. Following the phase-out of deposit ceilings, savings associations found the pursuit of high cost funds untenable and recognized the advantages of holding liquid securities in lieu of loans.[2] Faced with a rising cost of funds, lenders became net sellers of loans and looked to the secondary markets as a prime source of liquidity.[3] While savings associations were becoming more attuned to the secondary mortgage market, the demand for mortgage funds expanded greatly because of the strong growth in household formation, the increase in mobility of the population, the rise in housing prices, the increase in refinancing activity encouraged by accumulated equity and, recently, the decline in interest rates.[4] As the competition to satisfy a growing demand for mortgage funds intensified, lenders needed additional sources of funds to fulfill the need.

At the same time, continuing regulation of assets encouraged the liquidation of loan portfolios. Portfolio lenders were limited in the rate of growth on assets and were pressured to increase the ratio of capital to assets on their books. The secondary mortgage market stood ready to help with these problems.[5]

TABLE 1

Ownership of Mortgage Debt Outstanding
One- to Four- Family Non-Farm Dwellings

		Held by:			
Year	**Total (Billions)**	**Thrifts**	**Banks**	**Federal Agencies***	**Pools**
1977	$ 642.7	57.4%	16.4%	5.6%	9.4%
1978	753.5	55.7	17.1	5.8	10.1
1979	870.5	52.9	17.2	6.1	11.6
1980	963.9	50.6	16.6	6.4	13.3
1981	1,038.5	48.3	16.4	6.5	13.7
1982	1,074.7	42.6	16.2	7.2	18.0
1983	1,189.8	40.5	15.3	7.3	21.7
1984	1,319.4	40.1	14.9	7.4	23.0
1985	1,469.1	37.8	14.6	9.0	24.6
1986	1,698.5	32.9	13.9	7.5	30.6
1987	1,925.2	31.1	14.3	6.4	34.0
1988	2,115.2	30.6	14.8	6.2	34.1

* Government National Mortgage Association, Farmers Home Administration, Federal Housing Administration, Veterans Administration, Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Land Banks.

Source: *Federal Home Loan Bank Bulletin, Savings and Loan Source Book, Federal Reserve Bulletin*

Economic Factors

The successful deregulation of an industry that had long been accustomed to constraint was a product of extraordinary economic conditions. Namely, the rise and fall of inflation rates and the associated upheaval in interest rates had subjected the financial sector to unusual volatility and exposed the most serious flaw of the traditional mortgage lending system: the maturity mismatch between assets and liabilities. Lenders adopted two innovations to help solve this problem, both of which served to place more reliance on secondary mortgage markets. First, mortgage lenders made aggressive moves to originate adjustable rate mortgages in lieu of fixed rate loans. Many lenders found that, even with heavy discounts on ARM terms, they had to offer fixed rate loans as an alternative. They also found that originations of fixed rate loans could be sold into the secondary markets while ARMs could be retained in portfolio.[6] Second, portfolio lenders purchased mortgage-backed securities instead of holding whole loans because these securities qualified as

mortgage assets for tax purposes but could be readily liquidated in the market if a need for cash arose. The federally sponsored secondary mortgage market agencies encouraged this strategy by offering swap programs that traded securities for loans. In fact, the popularity of these swap programs was one key to the growth of the secondary mortgage market.[7]

Technology

Technological developments also served to expedite the linkages between loan originations and loan securitization. Computerized networks enhanced mortgage banking operations, and the secondary mortgage market agencies streamlined the processes of providing commitments and delivering loans.[8] These developments prepared the secondary market to handle ever growing volumes of business.

Factors That Deflect The Growth Trend

Although the secondary market appears to be poised for continued growth, David Seiders, chief economist for the National Association of Home Builders, has argued that several developments may deflect the trend: First, interstate mergers of failing institutions and the spread of branch banking are reducing the need for a secondary market to overcome geographic imbalance. A large multistate association may shift funds among branches to match supply and demand on a broad geographic scale. Second, because many associations have sold off most of their low-yielding fixed rate mortgages, the need for liquidity is diminishing, especially with a large proportion of lender portfolios comprised of ARMs. Third, associations are becoming more sophisticated in the techniques of issuing mortgage bonds and can take advantage of recent legal reforms that make issuance less cumbersome. The development of mortgage futures markets also is allowing lenders to hedge against volatile interest rates. Finally, the extent of the transformation of portfolio lenders into mortgage bankers may have been exaggerated. Seiders has pointed out that institutions are moving back to being net purchasers of mortgage loans after being net sellers of loans for several years.[9]

Not to be overlooked is the fact that the secondary mortgage market rose to prominence during a period of unusual growth in the demand for mortgage funds. In the late 1970s, national home ownership rates accelerated, while average home prices soared. The result was a great leap in the dollar volume of mortgage loans originated for home purchase. The general decline in mortgage interest rates, beginning in 1982, induced a surge in loan refinancing, including the refinancing of many expiring seller-financed loans. A large share of these refinanced loans was made by mortgage bankers, which added fuel to the growth of the secondary market. The effect of these events on the mortgage market has largely been realized; rapid growth in the demand for mortgage funds therefore is not expected to continue.

The secondary market has become an important part of the mortgage lending system and is likely to retain a major role. However, as the points discussed above suggest, the rapid recent growth of that market has been the result of a combination of extraordinary events and conditions and therefore is not likely to continue. Most likely in the near-term future is a state of coexistence between the agency-dominated secondary market and a financially stronger and sophisticated lending industry. However, this balance will depend on several factors:

- The impact of the Financial Institutions Reform, Recovery and Enforcement Act on loan originations at savings and loan associations. A crippled thrift industry could shift the home loan market toward mortgage bankers and commercial banks, thereby placing more emphasis on secondary market activities.
- The operation of federal secondary market agencies. Whether or not agencies become privatized could depend on the growth of the secondary market.
- The success of REMICs in opening opportunities for private secondary market issuers. This new mechanism for issuing mortgage-backed securities, created by the 1986 Tax Reform Act, reduces much of the rigidity that discouraged private mortgage conduits in the past.
- Resolution of the current shake-out in the market for mortgage-backed securities. The demand for securities is down amid investor concern about the soundness of mortgages in general. There is also fear that thrifts may cut back purchases of securities.[10] If the market has peaked, there will be little room for new issues.

A Future For Private Conduits?

Although federally-related agencies dominate the secondary mortgage market, there is a fledgling industry of purely private mortgage conduits that are surviving by finding unserved niches within the market. These private mortgage firms face important hurdles in attempting to compete with the agencies; however, recent legislation has reduced some of these hurdles.

The Secondary Mortgage Market Enhancement Act of 1984 eased several of the barriers faced by private firms by allowing issuers of investment quality mortgage-backed securities to use shelf registration with the Securities and Exchange Commission or blind pools (i.e., raise funds before acquiring specific mortgage loans) and by granting certain exemptions that previously had been enjoyed only by federally-related agencies, including exemption from state "blue sky" laws. It has been estimated that these changes save private issuers about two basis points in issuance costs.[11]

The 1984 act also broadened the market for private mortgage issues. Regulations were changed to allow purchase of private mortgages by pension funds and savings and loan associations.[12]

The creation of REMICs in 1986 provided further flexibility. Tax and accounting problems were eliminated by allowing use of sale of assets treatment without tax

liability at the issuer level. Administrative control was increased by eliminating the need for a financial subsidiary to issue the securities. Ending the requirement for overcapitalization made issuance more profitable. From a legal standpoint, private firms were placed on equal footing with the federal agencies.

Competition With Federal Agencies

Regardless of the improved operating environment for private firms, they still must compete with the formidable federal agencies. Private firms are unable to offer comparable yields for the purchase of mortgage pools; rather, they must limit activity to "non-conforming" loans, or loans with principal amounts above the statutory limits placed on the agencies. Still, the non-conforming segment of the market is relatively small.[13]

Competitive problems stem from two basic sources. The federal agencies enjoy the implicit backing of the U.S. Treasury, which creates the perception among investors that their issues hold low risk and reduces the interest rates the agencies must pay on security issues.[14] Second, the massive market volume of agency operations provides a measure of market power and economies of scale.[15]

These two problems were addressed by the Reagan Administration, whose policy toward secondary mortgage markets was to encourage private participation, if not to advocate complete privatization of the market. Attempts were made to counter the implicit backing of the agencies by the Treasury by requiring the agencies to pay user fees on each security issued. The idea was that the fee would match the value of the implicit Treasury guarantee and make the issue fully priced in a competitive market.[16] However, such fees would raise costs to the agencies and lower the prices they could pay for mortgage loans. Because of the major role the agencies play in providing liquidity for residential loans, the ultimate result would be higher mortgage interest rates to the home buyer. So far, strong opposition from the mortgage industry has succeeded in frustrating user fee proposals.

Attempts to stem the growth of the agencies have been less clear cut. During the formulation of legislation creating REMICs, some opposition was expressed against allowing the agencies to use the new device. However, the philosophy that prevailed was one of helping the private issuers without hurting the agencies by limiting their participation, especially since REMICs were expected to be the predominant vehicle for issuing mortgage-backed securities.[17] As a trade-off, the Department of Housing and Urban Development authorized the Federal National Mortgage Association to issue REMICs only after agreeing to study the issue of privatization. A special task force on the issue recommended the creation of two entities, one that would continue FNMA's current support of the housing financing market and another that would be completely independent.[18] The report also emphasized that a private FNMA would not be feasible if the Federal Home Loan Mortgage Corporation remained tied to the government. However, this was the extent of the effort; the change to the Bush Administration and the FSLIC crisis shifted attention away from the issue.

The Issue Of Privatization

On the surface, this issue appears to be one of ideology which, if true, would hold only casual interest for those participating in mortgage markets. The extent of privatization does, however, hold practical importance as well.

Proponents of privatization point out that the original purpose of federal agency participation in the home loan markets was to organize and facilitate a market structure that was fragmented at best. For many years, the agencies carried on small-scale operations because their purchase offers were relatively uncompetitive. During volatile recent times, the agencies became very competitive bidders for loans, and they grew accordingly. Continuation of this growth is seen as a threat to depository institutions and established roles in the primary as well as the secondary mortgage markets. Some see the eventual demise of the traditional portfolio lender as loans are originated primarily for sale in the secondary market and a housing market that would lose an important buffer against the inherent volatility of the capital markets.[19]

Opponents of privatization emphasize the costs of losing the participation of the agencies. They assert that private firms could not compensate for any substantive agency withdrawal from the market. Without federally supported agencies, mortgage securities would be viewed as more risky, thus raising interest rates on mortgage originations.[20] A private FNMA would not need to confine itself to housing financing and, when profitable, could shift to other areas of investment. Therefore, the old problem of disintermediation could return. Smaller lenders, lacking the volume needed to directly access capital markets, would lose the advantages of the secondary market.[21]

The issue of privatization revolves around two differing perceptions of the agencies: one, as threats to the traditional system of making mortgage loans; two, as essential ingredients in protecting the mortgage loan system. Resolution of the issue appears to hinge on the prospects for continued growth of the secondary market. If the market expands further and the agencies grow along with it, the controversy will intensify. Conversely, if the market stabilizes and matures, the issue may become moot.

It is reasonable to expect "privatized" agencies to operate much as federal agencies do now. Even if privatized, the agencies, by their very size, would continue to enjoy competitive advantages in the areas they operate. Furthermore, privatization would free the agencies to encroach on the niches carved out by private mortgage conduits. However, a more accurate accounting of the real cost of securitizing mortgages might force the housing industry to compete more effectively for funds with other sectors of the economy.

Securitization Of A Broader Array Of Loans?

The secondary mortgage market has been very successful in securitizing fixed rate mortgage loans on single-family

homes largely because of standardization of the product. From a risk standpoint, homes are relatively similar, and mortgage underwriting procedures also are similar, in part because lenders accept guidelines from the federal agencies to assure a market for the loans. Guidelines were established initially by the Federal Housing Administration, but lately the secondary market agencies have established their own rules for making conventional loans.[22]

Traditional single-family home loans are only part of the real estate debt held by financial institutions. Financial institutions also hold loans for homes financed with adjustable rate mortgages and 15-year fixed rate loans. In addition, the institutions hold loans for multi-family projects, mobile homes, condominiums and various types of non-residential properties. Although some entrees have been made, securitization of these forms of debt has been lagging.

The apparent reluctance to extend securitization stems from the difficulties in assessing risk for pools of loans with varying characteristics. After all, a bond is a relatively dependable investment; it provides a fixed income over a predictable period of time. Property loans, in contrast, introduce much more uncertainty. The property may turn out to be a poor performer; property values may decline, or the borrower may encounter economic difficulty. Also, unlike major corporations or governmental entities, most mortgage borrowers have limited capacity to weather adverse financial conditions. Because of these uncertainties, the risk of default on property loans is significant.

An additional source of uncertainty involves prepayment of loans. Most mortgage loans allow the borrower to repay the loan balance at his discretion. Typically, borrowers refinance loans when interest rates fall. Unfortunately for the holder of the mortgage, that is the worst time to recover the principal of the loan, since proceeds must be reinvested at a lower rate of return.

If the probability of loan default and prepayment can be estimated, the financing market may discount the price of the security by an appropriate amount to compensate. This estimation has been accomplished, with some proficiency, for fixed-rate, single-family home loans. Default insurance is readily available on the individual loans from FHA and private insurers; guarantees of timely payment at the pool level are provided by the Government National Mortgage Association or the issuer. Because of lenders' long experience with these types of loans, insurers are willing to undertake the risk of default, and investors have a basis for assessing prepayment risk. However, other types of loans are either too new or too complex to lend themselves to reliable estimation. ARMs provide a good example.

Adjustable Rate Mortgages

When ARMs became widely available in the early 1980s, the various combinations of adjustment terms, indexes and other features produced a vast variety of loan types. However, since most lenders retained ARMs in their portfolios, this variety was not too much of a problem. As the volume of ARMs rose, the need for securitization of ARM loans increased. In response, the federal secondary mortgage market agencies identified a short list of ARM characteristics they would buy. However, because of the newness of the product, the agencies did not know what to expect from even the limited types of ARMs they purchased.

In simulations and actual practice, it has been found that certain features of ARMs affect default risk and prepayments significantly. The loans often are originated at deeply discounted interest rates in order to attract borrowers away from fixed rate loans. Many lenders qualify borrowers based on the low first year rate, leading to delinquencies when the rates are later increased. At times of interest rate volatility, adjustment caps have helped limit borrower defaults. However, experience is insufficient to evaluate the effect of these factors on credit risk.[23] The agencies are addressing these problems by promulgating specific underwriting guidelines in a manner similar to those on fixed rate loans. In the process, they are bringing a level of standardization to ARMs.

Loans For Multi-Family Units

Multi-family housing is another area in which the secondary mortgage markets have made limited inroads. Freddie Mac began issuing multi-family pass-through certificates in 1984. Since then, there has been a steady increase in agency involvement. (Table 2 shows the small, but increasing, portion of all multi-family unit debt held in agency pools.) In 1987 Freddie Mac purchased $2 billion and Fannie Mae purchased over $300 million of multi-family unit loans.

TABLE 2

Multi-Family Unit Mortgage Debt
Held in Agency Mortgage Pools

Year	Total Debt (Billions)	GNMA (Billions)	FHLMC (Billions)	FNMA (Billions)
1985	$214.0	$4.9 (2.3%)	$0.9 (0.4%)	$1.0 (0.4%)
1986	247.8	5.8 (2.3)	4.7 (1.9)	1.4 (0.6)
1987	273.9	7.7 (2.8)	6.7 (2.4)	2.0 (0.7)
1988	287.6	9.3 (3.2)	6.5 (2.3)	5.9 (2.1)

Source: *Federal Reserve Bulletin*

The problem of assessing the risk of default and inopportune prepayment is even more acute with multi-family unit loans. Not only are the properties heterogeneous, but underwriting methods often are customized to specific loan situations. The amount and terms of a loan depend on the projected performance of the property rather than on the credit-worthiness of the borrower. Moreover, financing arrangements are varied, including participation loans with various types of kickers to the lender.[24] Unlike

loans on owner-occupied homes, there are no data on prepayments.

Income property loans have been sold to investors in the past. Because single loans may be large, they may be sold off individually. Forming pools for the purpose of securitizing the loans is impeded by the lack of standardization. Recent developments may overcome the problem. Standard and Poor's now provides ratings for pools of commercial property loans.[25] Freddie Mac has developed a method of risk-based pricing which is sensitive to underwriting standards.[26] In addition, some conduits are self-insuring the pool by taking a subordinated interest.[27]

There are other areas of real estate financing that have not been introduced to securitization, such as loans for manufactured housing, second homes and net lease properties.[28] Apparently, these areas are constrained only by the problem of assessing risk because there are plenty of loans available to form pools.

Moral Hazard Problems

While broadening the base of securitized real estate debt may offer a more reliable supply of financing, some are concerned about the moral hazard problems that may ensue,[29] that is, the possibility that loan originators may be tempted to maximize loan volume at the expense of quality, knowing that the problem will be someone else's. This problem is recognized by secondary mortgage market operators and is a reason why they promulgate standards for underwriting loans. The real question is whether standardization will work in an area of financing that requires flexibility for a successful transaction. Real estate investors may find it difficult to negotiate terms with a lender whose allegiance is to Wall Street.

Undoubtedly, there will be continued experiments in securitizing various types of real estate debt. Some will be successful, while others will not. So far, innovators have moved with caution, so that no major security crises have occurred, and there is little reason to expect this situation to change.

Is The Secondary Market A Threat To Traditional Mortgage Lenders?

The 1970s and 1980s have been years of turmoil for housing financing. Volatile economic change has exposed the weaknesses of the mortgage origination system. Growth of the secondary market has largely been responsible for preventing collapse of the system. The secondary mortgage market has alleviated some of the old problems of portfolio lenders. By providing an alternative source of loanable funds, the secondary market has filled the gap caused by disintermediation in the face of rising short-term interest rates. By providing liquidity in lender portfolios, the secondary market has alleviated the problem of asset-liability mismatching.

Yet some feel that, by stepping in to save the system, the secondary mortgage market may have planted the seeds of the eventual demise of mortgage originators as they presently exist. There is no question that secondary mortgage market operations have changed the overall mortgage market. Whether that change will transform the function of lenders is open to question.

Increased Specialization

One result of the rise of secondary markets is increased specialization in the process of delivering mortgage funds to borrowers. Lenders may concentrate on the origination process as a profit center apart from earnings from the loans themselves; they need not undertake the liabilities of holding loans.[30] This has blurred the distinction between institutional lenders and mortgage bankers. Portfolio lenders may hold mortgage-backed securities and still qualify for favorable tax treatment. Even servicing contracts may be sold in the market to provide up-front cash flow. A whole industry has developed around the firms specializing in servicing mortgages.[31]

The movement toward specialization not only liberates the traditional lender from the problems of holding mortgages, it also provides alternatives to the lender's participation. Liquidity provided through the secondary market has been instrumental in encouraging more long-term mortgage lending at commercial banks.[32] Furthermore, there may not be a need for a lender to be involved; builders and real estate brokers may originate mortgages directly with credit market conduits through computerized networks.[33] Borrowers may feel more comfortable dealing with traditional lenders until they realize that it makes little difference who makes the loan when they are dealing with a servicing firm in some distant city while their loan is being held in a credit pool that is even farther removed.

Standardization Of Underwriting And Mortgage Instruments

The secondary markets have been instrumental in standardizing loan underwriting and mortgage instruments.[34] Such factors as loan qualifying standards and appraisal forms promulgated by FHLMC and FNMA have become fixtures in the industry. To an increasing degree, loan terms that are acceptable in the secondary market also are offered in the primary market. Even portfolio lenders want to retain the options afforded by a marketable loan. While such standardization has brought some order to the market, it also may have stemmed the innovation in mortgage design that emerged immediately after deregulation. Although economic stability has been a big factor, standardization of mortgage loans has had the effect of reducing the types of mortgages that are available. The menu of mortgages available to the borrower today is not the smorgasbörd it was a few years ago.

Possibly of greater concern than the loss of innovation in mortgage design is the trend toward reducing the underwriting responsibility of mortgage originators. If lenders see their role as merely satisfying a list of standard criteria

established by secondary mortgage market agencies, neither investors nor borrowers will be well served. The agencies recognize this threat and have acted to discourage some practices that erode the quality of loans. Their greatest weapon, however, is the removal of the loan originator's access to the market by refusing to purchase further loans when a pattern of bad loans develops.[35]

Securitization

Securitization programs have reduced risks significantly for portfolio lenders. By swapping whole loans for securities, lenders add liquidity to their portfolios.[36] Using these mechanisms is a necessity in a market in which interest rates are subject to wide swings. The growing relationship between lenders and secondary investors places less emphasis on individual borrowers and depositors. The concept of the self-sufficient community savings and lending institution is becoming obsolete.

Some see the real threat to primary lenders on the liability side. The agencies' securitization process is seen as a more efficient way of doing what savings associations do—convert investors' funds into mortgage credit. The associations' ability to raise funds may become limited to retaining small, conservative depositors.[37] At that point, savings and loan associations would be little different from mortgage bankers.

Finally, the full development of secondary markets opens up a vast source of funds for mortgage loans.[38] What has been sacrificed is the stable mooring of low cost deposits as a base for mortgage interest rates. These rates now move in a fashion that is similar to the movement of credit yields,[39] and mortgage loans are rationed by interest rate levels rather than by supply. While this development may appear to be beneficial, in actuality, the economy loses the traditional role of housing as a counter-cyclical leader during business recessions.

Conclusion

It is tempting to view change as the loss of something valuable. The integration of the local mortgage lender into the broad securities markets may strike some as unfortunate. Certainly, the ultimate holder of mortgage loans has no commitment to the local area, and mortgage lending is no longer a matter of pooling local resources for local needs. In many ways, this development is similar to the demise of the mom and pop grocery. While some aspects of the relationship between lender, depositor and borrower may have been lost, opportunities and options for lenders, borrowers, investors and suppliers of specialized services have been increased. In economic terms, increased options generally promote greater initiative, efficiency and responsibility. Therefore, the change brought about by the development of the secondary mortgage market must be seen as a benefit to society, however uncomfortable it may be for those who are unprepared for change or for those who have entrenched interests.

NOTES

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