

market commentary

WANT BETTER YIELDS ON YOUR AGENCY MBS PURCHASES?

Consider MPF mortgage participations

FHLBank Topeka members have the opportunity to participate in mortgages that are sold under the MPF Program, which although not fully guaranteed, have a similar credit profile to agency MBS securities.

The MPF mortgages are backed by a credit enhancement provided by the originator/servicer and enforced by FHLBank Topeka. In addition, the loans offer higher yields based on the purchase price and prepayment characteristics. The following analysis compares recent MPF production to the TBA agency MBS market and illustrates the yield and spread improvement that can be achieved through MPF participations.

The tables below compare the transaction details for the MPF mortgages and MBS securities using recent MPF loan production and a comparable Fannie Mae MBS security.

MPF Mortgages vs. MBS Securities

MPF MORTGAGES

TRANSACTION DETAIL	
Transaction Size	10,215,020
Asset Term	30 years
Note Rate	3.88%
Expected Asset Yield	2.96%
Expected Funding Cost	2.09%
Initial Spread	0.86%

MBS Security

TRANSACTION DETAIL	
Transaction Size	10,271,501
Asset Term	30 years
MBS Coupon	3.00%
Underlying Collateral	3.75%
Expected Asset Yield	2.57%
Expected Funding Cost	1.94%
Initial Spread	0.63%

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**RESIDENTIAL
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Find out more about Jenny and our funding specialists at **FHLBTOPEKA.COM/INTELLIGENCE.**

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The MPF mortgages have a weighted average note rate of 3.88% and were purchased at a weighted average price of 102.0522. The MBS security has a coupon of 3.00% and underlying mortgage collateral with a note rate of 3.75%. The security traded at a price of 102.5625.

The expected asset yield is driven by the price and corresponding premium paid as well as the speed at which the mortgages prepay in a base case or stable interest rate environment as determined by the models FHLBank Topeka uses to estimate prepayment speeds and measure interest rate risk. We also used these same models to run 1,000 interest rate scenarios to determine a funding approach that provides good risk adjusted returns based on the transaction spread and net duration mismatch between the assets and advance funding.

The linked analysis at the bottom right illustrates the expected asset yields in different interest rate scenarios where faster or slower prepayment speeds impact the amortization of the premium paid on the assets. Higher interest rates and slower prepayments generally result in increased yield because of lower premium amortization.

The funding strategy detailed in the analysis is generally the same for both assets and consists of a blend of fixed rate and callable advances. The Advance Summary section illustrates a weighted average funding cost on the MPF mortgages that is slightly higher because of the longer term callable advances used in the funding mix. The MBS strategy has increased reliance on longer term fixed rate advances (20 year). Both approaches produce fairly conservative net duration mismatches in different interest rate scenarios.

The net duration mismatch for both transactions is slightly positive as rates rise, which produces slightly wider transaction spreads. Both transactions also benefit from the ability to call, or prepay without fee, the callable advances in a declining interest rate environment with wider spreads in the -100 scenario than in the base case.

While both sample transactions are well hedged and provide wider transaction spreads in both falling

and rising interest rate scenarios, the MPF mortgages deliver wider spreads than the MBS security. **This is primarily because of continued wide spreads between primary and secondary market yields that are driven by the large guarantee fees being charged by FNMA and FHLMC.**

The tables below compare the transaction spreads on the two investment alternatives with the MPF mortgage strategy providing an average spread pick-up of another 25 basis points. The pickup becomes greater as interest rates rise.

MPF Spreads Lead MBS by 25 bps

MPF MORTGAGE SPREAD SUMMARY				
Syr Average	-100	0	100	200
Asset Yield	2.56%	2.95%	3.22%	3.34%
Liability Cost	1.34%	2.09%	2.15%	2.21%
Spread	1.23%	0.85%	1.07%	1.12%
Average Spread	1.07%			

MBS SECURITY SPREAD SUMMARY				
Syr Average	100	0	100	200
Asset Yield	2.24%	2.58%	2.83%	2.94%
Liability Cost	1.14%	1.94%	2.06%	2.17%
Spread	1.10%	0.64%	0.77%	0.77%
Average Spread	0.82%			

Other advantages to buying participations in MPF mortgages are the ability to grow your institution's loan portfolio, invest in high quality assets that provide substantial protection from credit losses through the provided credit enhancement and the ability to achieve greater geographic diversification from loans originated outside your market. FHLBank Topeka administers all aspects of the MPF Program including managing the mortgage servicing and mortgage payments as well as ongoing quality control reviews and the enforcement of origination rep and warrant violations.

see our full analysis:

30-year Funding Strategy - MPF

30-year Funding Strategy - MBS

Contact your account manager today to find out more about MPF mortgage participations.

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