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Mandatory versus Best Efforts Pricing Comparison

The chart below provides a comparison of the base pricing for different types of loan deliveries. On the left hand side are the 30 year fixed rates, starting with 4.125% and ending with 4.750%. The next column contains the actual market price, which is the price a loan can be sold directly to a broker or dealer. The remaining columns list mandatory and best efforts pricing on a single day for a large aggregator and one of the agencies. Lenders who sell loans using MBS securities execute their sales at the market price. Other lenders must obtain pricing from the agencies or the aggregators.

30 Year Fixed Rate Base Pricing (SRP not included)					
Note Rate	Market Price	Agency Mandatory	Agency Best Efforts	Aggregator Mandatory	Aggregator Best Efforts
4.125%	100.14	100.06	99.560	99.510	98.014
4.250%	100.53	100.48	99.980	99.850	98.360
4.375%	100.56	100.89	100.39	100.04	98.569
4.500%	101.16	101.26	100.74	100.35	98.892
4.625%	101.76	101.60	101.10	100.59	99.138
4.750%	102.15	101.95	101.45	100.74	99.290

Mandatory Pricing

For purposes of this comparison, pricing is examined and discussed for only one rate. On this day, the actual market price for a 4.250% loan was 100.53. The Agency Mandatory price was 100.48 (at the market price allowing for timing difference). *The Agency pricing referred to in this chart is available only for lenders selling directly to the agency, not to an agency designated third party.*

Aggregator Mandatory pricing is 68 basis points lower than the actual Market Price. This is largely because rates are at a historic low, putting pressure on servicing values. Most aggregators adjust their base pricing downward during periods of declining servicing values, instead of adjusting their servicing released premiums.

Best Efforts Pricing

Generally, Agency and Aggregator Best Efforts Pricing is 35 to 50 basis points lower than their respective mandatory pricing. In the example above, the Agency Best Efforts Pricing is 50 basis points worse than its mandatory pricing. The Aggregator Best Efforts Pricing is 150 basis points lower than its mandatory pricing and 200 plus basis points lower than the actual market price.

Best Execution

The base pricing only tells part of the story. To determine the best execution for the lender, the total or

“all-in” price must be examined. This price includes the base price plus the servicing released premium, or SRP.

Best Execution Analysis

Assume the lender will sell 25 basis points of servicing simultaneously with the sale of the loan. The servicing values in the chart below are actual values obtained on the same day as the loan pricing. On this date, the lender could sell the loan to the agency via Best Efforts or Mandatory delivery and sell the servicing at 1.25. The lender also has the option to sell the loan to the aggregator via Best Efforts or Mandatory delivery and sell the servicing at 1.90. By combining the base prices from the previous chart and the associated SRPs, we arrive at the total (all-in) pricing shown below.

Note Rate	Agency 30 Year Fixed Rate Pricing						Aggregator 30 Year Fixed Rate Pricing					
	Mandatory			Best Efforts			Mandatory			Best Efforts		
	Base Price	SRP	Total Price	Base Price	SRP	Total Price	Base Price	SRP	Total Price	Base Price	SRP	Total Price
4.125%	100.060	1.25	101.310	99.560	1.25	100.810	99.510	1.90	101.410	98.014	1.90	99.914
4.250%	100.480	1.25	101.730	99.980	1.25	101.230	99.850	1.90	101.750	98.360	1.90	100.260
4.375%	100.890	1.25	102.140	100.390	1.25	101.640	100.040	1.90	101.940	98.569	1.90	100.469
4.500%	101.260	1.25	102.510	100.740	1.25	101.990	100.350	1.90	102.250	98.892	1.90	100.792
4.625%	101.600	1.25	102.850	101.100	1.25	102.350	100.590	1.90	102.490	99.138	1.90	101.038
4.750%	101.950	1.25	103.200	101.450	1.25	102.700	100.740	1.90	102.640	99.290	1.90	101.190

A best execution analysis is performed by comparing the total price for each delivery method. The best execution for each note rate is highlighted in bold print and noted under the Best Execution column in the chart below.

Note that the price for Agency Mandatory Delivery and Aggregator Mandatory are about the same. The aggregator’s lower base price is offset by its higher servicing released premium. Agency Best Efforts is superior to Aggregator Best Efforts. This reflects the severity of the Aggregator base price reduction. Aggregator Best Efforts Total Price is 100-150 basis points worse than the other executions.

This chart provides pricing for one day only, but is representative of the increased profitability that can be generated by selling loans via mandatory delivery. Mandatory delivery execution has been substantially better than best efforts execution for the past two years. This trend is expected to continue.

30 Year Fixed Rate Total Pricing (Base + SRP)					
Note Rate	Agency Mandatory	Agency Best Efforts	Aggregator Mandatory	Aggregator Best Efforts	Best Execution
4.125%	101.310	100.810	101.410	99.914	101.410
4.250%	101.730	101.230	101.750	100.260	101.750
4.375%	102.140	101.640	101.940	100.469	102.140
4.500%	102.510	101.990	102.250	100.792	102.510
4.625%	102.850	102.350	102.490	101.038	102.850
4.750%	103.200	102.700	102.640	101.190	103.200

Requirements

The threshold to switch from best efforts to mandatory delivery is generally pegged at \$15-\$20 million in sustainable conventional 30 year agency business per month. Other requirements include:

- Fallout Tracking.
- Discipline and Attention to detail.
- Working knowledge of pipeline behavior.
- Customer knowledge.
- Pipeline management reports.
- Management tolerance for fluctuations in gain on sale during market volatility.
- Warehouse capacity to hold closed loans for a period of time to obtain a best execution price.