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Bank Watch

ARTICLE

Mortgage Banking's Next Chapter: Is a Recovery Taking Root?

In This Issue

Mortgage Banking's Next Chapter: Is a Recovery Taking Root?

A little over four years ago, we published a two-part series entitled **Mortgage Banking Lagniappe** (Lagniappe is the Cajun word for "bonus" or "a little extra") as all-time lows in rates powered big mortgage earnings for banks and non-banks. Since then, a multi-year hangover has developed that causes us to ask: do rates have to fall materially for mortgage bank earnings to "normalize" and begin to contribute to bank earnings?

Figure 1, on the right, shows the level of and trends in key housing/mortgage data for 2024 and the Mortgage Banking Association's (MBA) three-year forecast.

Like many forecasts, our observation of the MBA forecast tends to suffer from recency bias. Around year-end 2023, MBA's forecast for 2024 projected a much stronger year than occurred because mortgage rates did not decline much even though the Fed cut its overnight policy rates by 100bps.

As a result, housing starts and sales of existing new homes were well below MBA's forecast. However, the median price of existing homes was $406 thousand at year-end 2024, which equated to a 4.5% increase from the year prior and exceeded the 4.1% forecast increase.

Although inventories of unsold homes are increasing and in some areas are surging, MBA expects home prices to increase modestly in the coming three-year period as mortgage rates are projected to remain in the mid-6 range for a 30-year mortgage. By 2027, home sales are expected to be 12% above 2024 reported figures while mortgage volume is expected to increase nearly 40% as the refi-share picks up. If that comes to pass, mortgage banking earnings may transition to being accretive to commercial bank earnings.

Figure 1:: MBA Forecasted Mortgage Activity

	Actual 2024	Forecast* 2024	Forecast 2025	Forecast 2026	Forecast 2027
Housing Measures					
Housing Starts (SAAR, 000)	1368	1424	1363	1375	1427
Single-Family	1014	1051	1015	1064	1123
Two or More	354	373	348	311	304
Home Sales (SAAR, 000)					
Total Existing Home	4076	4311	4259	4457	4585
New Homes	687	755	714	770	787
FHF US House Price Index (YoY % Change)	4.50%	4.10%	1.30%	0.30%	0.30%
Median Price of Total Existing Homes ($000)	406	390.5	412	415	416
Median Price of New Homes ($000)	422	432.5	424	426	431
Interest Rates					
30-Year Fixed Rate Mortgage	6.6%	6.1%	6.7%	6.4%	6.4%
10-Year Treasury Yield	4.3%	3.8%	4.4%	4.3%	4.3%
Mortgage Originations ($B)					
Total 1-to-4 Family	1779	2001	2076	2360	2455

** Data from February 2024 MBA Forecast*
Source: Mortgage Bankers Association

Mortgage rates were around 20% briefly in the early 1980s. Conversely houses were much cheaper. The analysis in Figure 2, on the next page, compares mortgage interest expense (using 30-year average mortgage rates and median U.S. transaction prices) to median household income, since the early 1980s.

As shown, housing was the most expensive at the beginning of this analysis when interest rates were in the mid-teens but trending lower. From 1984 to 1994, affordability improved as housing prices and income increased in-step but rates were nearly cut in half. From 1994 until the beginning of the GFC, relative affordability hugged the median (3.4x) as income and home prices, again, increased together while mortgage rates ranged from 6%-8%.

From the GFC until COVID, income growth outpaced the increase in housing prices while interest rates nearly halved, leading to improved affordability though post-GFC "reforms" made it more difficult to obtain a mortgage.

During COVID, the Fed engineered a sharp drop in long-term rates mortgage rates by buying over $2 trillion of Agency MBS. As a result, home prices skyrocketed but affordability as measured by household income as a multiple of mortgage interest expense rose to nearly 7x vs. a long-term average of 3.4x.

This was a bit of a mirage since 30-year mortgage rates for a while were below 3%; today it is around 6.5% after peaking near 8% in 2023. With normalization of rates since 2022, the household income-to-mortgage interest expense ratio has fallen back to near the long-term average of 3.4x yet housing is unaffordable for many.

So, it may take further increases in housing supply and a mild (or worse) recession to push mortgage rates lower and power a pick-up in mortgage refinancing and origination activity that would thereby drive better mortgage earnings. Some combinations of the following might work: rates down to the high 5s, housing prices decline 10-15%, or income increases 15-20%.

An additional technical factor in the market is working against an improvement in mortgage rates and therefore earnings derived from mortgage banking is the spread between the 10-year UST and mortgage rates.

During the past 40 years, the average spread was 175bps. Once the Fed engaged in "Quantitative Easing" in the post GFC years, the spread began to widen; however, it has gapped to around 250bps the past couple of years as MBS investors are concerned about the potential for the Fed to become an insensitive seller as it presumably needs to shrink its Agency MBS portfolio to make room for more USTs. A return to the 175bps spread average would, all else equal, cause mortgage rates to fall below 6%.

Figure 2:: Median Household Income vs. Mortgage Interest Expense

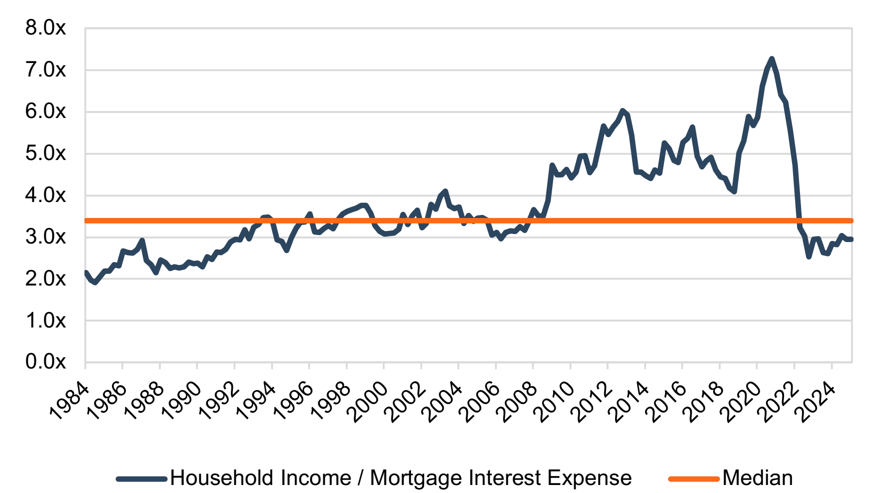
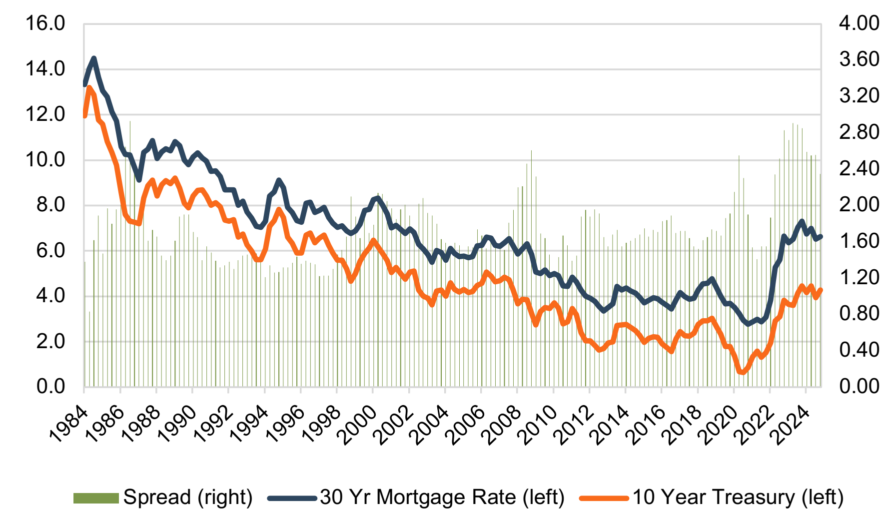


Figure 3:: 30-Year FHLMC Mortgage Rate vs. 10-Year US Treasury Yield



Source: Federal Reserve

One result of the GFC reforms is that non-bank mortgage companies now originate the majority of residential mortgages. The data in Figure 4 succinctly summarizes the impact of falling and rising rates on origination volumes and gain on sale margins. Not shown is the share of originations that are refinancings, which, since 2022, when rates began to rise, are very low (and consumers switched to draws on HELOCS). Nonetheless, 2024 was somewhat better than 2023 when long-term rates peaked and 2025 may be somewhat better than 2024.

Figure 4:: Mortgage Originations and GOS Margins

	Originations ($M)	Indexed Originations; 2019=100					
Company	**2019**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Rocket	145,180	100	221	242	92	54	70
UWM	107,767	100	169	210	118	100	129
LoanDepot	45,324	100	222	302	119	50	54
Guild	21,848	100	161	169	88	70	110

	Gain on Sale Margins					
Company	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Rocket	3.19%	4.46%	3.13%	2.82%	2.63%	2.95%
UWM	na	2.49%	1.14%	0.77%	0.92%	1.10%
LoanDepot	2.77%	4.13%	2.61%	1.63%	2.60%	2.96%
Guild	3.78%	5.00%	4.02%	3.68%	3.40%	3.32%

Source: Company SEC filings

A vote of confidence in the future of mortgage banking has been registered by the largest originator, Rocket Companies, Inc. (NYSE:RKT). On March 10, 2025 RKT announced a $2.4 billion acquisition of Redfin Corporation (NASDAQ:RDFN), the online real estate brokerage business with 50 million monthly viewers. RKT then announced a $9.4 billion acquisition of Mr. Cooper Group Inc. (NASDAQ:COOP), bringing together the largest mortgage originator and servicer in the nation, on March 31. Consideration paid to both RDFN and COOP shareholders will consist solely of RKT common stock, which will result in about 25% ownership dilution to RKT shareholders.

The transaction may signal the bottom is in or maybe was put in 2023 with better times to come for mortgage banking and banks that have meaningful mortgage banking units.

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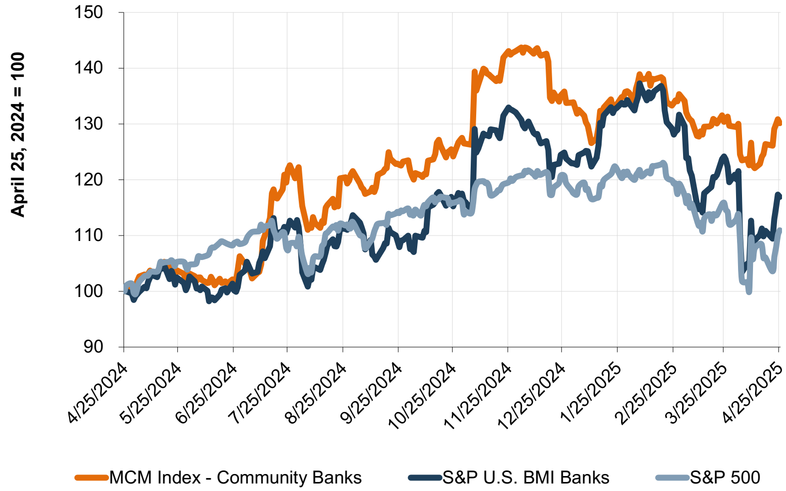
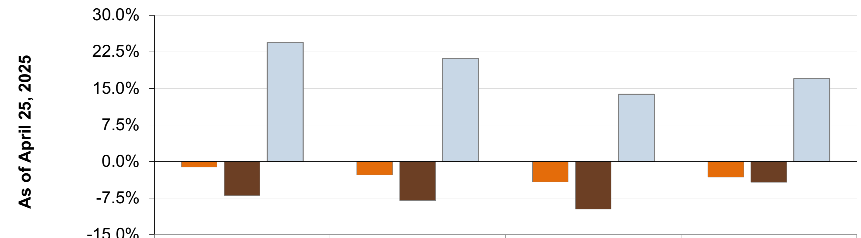
Mercer Capital's Bank Group Index Overview



Source: S&P Capital IQ Pro.

Return Stratification of U.S. Banks

by Market Cap



	S&P U.S. Banks Market Cap Under $250 Million	S&P U.S. Banks Market Cap Between $250 Million - $1 Billion	S&P U.S. Banks Market Cap Between $1 Billion - $5 Billion	S&P U.S. Banks Market Cap Over $5 Billion
Month-to-Date	-1.13%	-2.78%	-4.24%	-3.22%
Year-to-Date	-7.04%	-8.06%	-9.78%	-4.31%
Last 12 Months	24.40%	21.10%	13.79%	16.95%

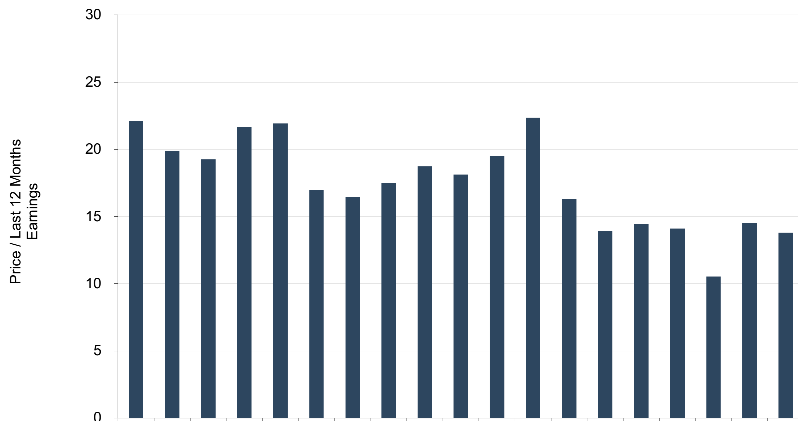
Source: S&P Capital IQ Pro.

	Total Return			Regional Index Data as of April 25, 2025					
	Month-to-Date	**Year-to-Date**	**Last 12 Months**	**Price / LTM EPS**	**Price / 2025 (E) EPS**	**Price / 2026 (E) EPS**	**Price / Book Value**	**Price / Tangible Book Value**	**Dividend Yield**
Atlantic Coast Index	-2.0%	-6.7%	29.3%	10.7x	10.4x	8.8x	104%	110%	2.9%
Midwest Index	1.3%	-2.5%	30.3%	11.7x	9.3x	9.0x	97%	118%	2.8%
Northeast Index	3.0%	-1.3%	33.9%	10.7x	8.9x	7.7x	101%	118%	3.4%
Southeast Index	-1.3%	-1.8%	33.2%	10.4x	9.3x	7.8x	92%	107%	2.3%
West Index	-1.0%	-7.2%	22.7%	11.8x	9.9x	8.5x	91%	111%	3.3%
Community Bank Index	0.5%	-2.8%	30.1%	10.9x	9.4x	8.3x	97%	113%	3.0%
S&P U.S. BMI Banks	-3.3%	-4.9%	16.9%	na	na	na	na	na	na

Source: S&P Capital IQ Pro.

Median Price/Earnings Multiples

Target Banks' Assets <$5B and LTM ROE >5%

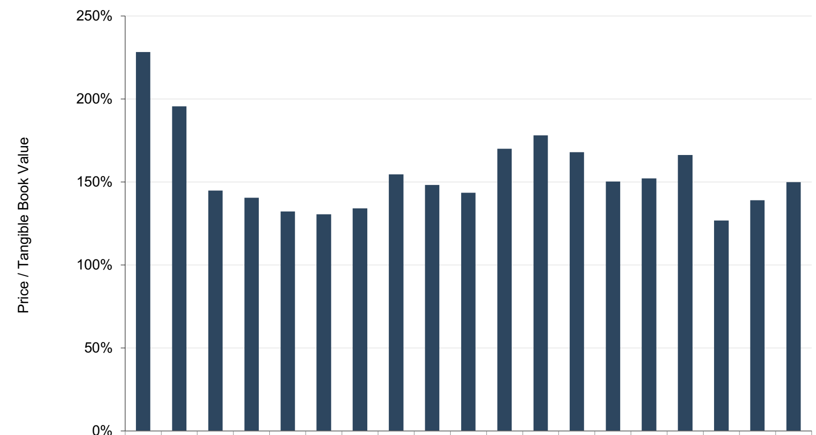


	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	LTM 2025
U.S.	22.1	19.9	19.3	21.7	21.9	17.0	16.5	17.5	18.8	18.1	19.5	22.4	16.3	13.9	14.5	14.1	10.5	14.5	13.8

Source: S&P Capital IQ Pro.

Median Price/Tangible Book Value Multiples

Target Banks' Assets <$5B and LTM ROE >5%

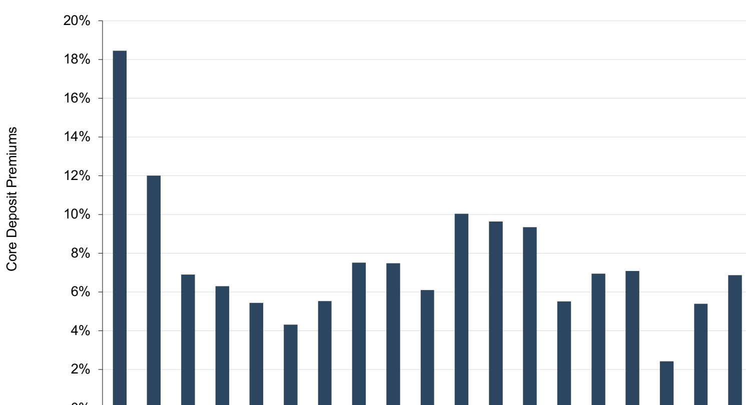


	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	LTM 2025
U.S.	228	196	145	141	132	130	134	155	148	143	170	178	168	150	152	166	127	139	150

Source: S&P Capital IQ Pro.

Median Core Deposit Premiums

Target Banks' Assets <$5B and LTM ROE >5%



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	LTM 2025
U.S.	18.4	12.0	6.9%	6.3%	5.4%	4.3%	5.5%	7.5%	7.5%	6.1%	10.0	9.6%	9.3%	5.5%	6.9%	7.1%	2.4%	5.4%	6.9%

Source: S&P Capital IQ Pro.

Median Valuation Multiples for M&A Deals

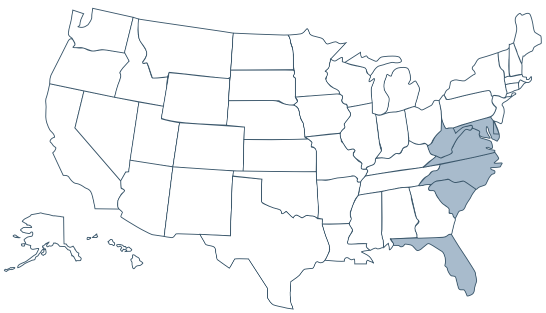
Target Banks' Assets <$5B and LTM ROE >5%, 12 months ended April 28, 2025

Regions	Price / LTM Earnings	Price/ Tang. BV	Price / Core Dep Premium	No. of Deals	Median Deal Value ($M)	Target's Median Assets ($000)	Target's Median LTM ROAE
Atlantic Coast	19.7x	169%	8.5%	4	150.4	828,948	9.6%
Midwest	13.8x	142%	4.0%	6	70.8	630,517	14.1%
Northeast	15.5x	133%	3.1%	7	236.2	2,257,367	8.3%
Southeast	9.8x	157%	10.4%	5	206.0	1,192,160	16.5%
West	17.7x	154%	9.1%	4	61.1	836,229	7.7%
National Community Banks	13.8x	150%	6.9%	26	106.0	969,174	11.0%

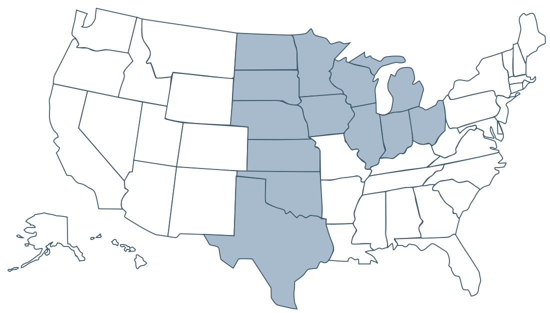
Source: S&P Capital IQ Pro.

Mercer Capital's Regional Public Bank Peer Reports

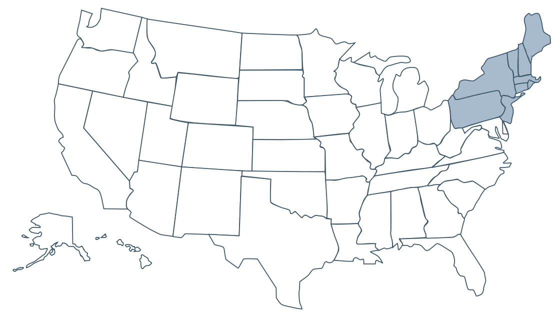
Updated monthly, Mercer Capital's Regional Public Bank Peer Reports offer a closer look at the market pricing and performance of publicly traded banks in the states of five U.S. regions. Click on the map to view the reports from the representative region.



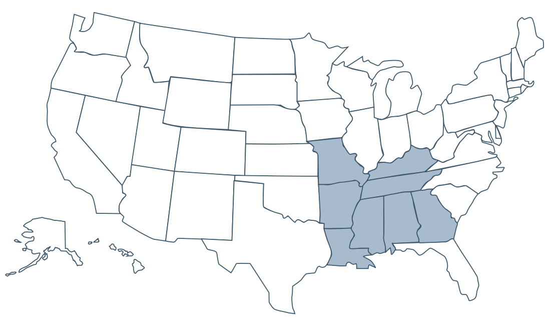
Atlantic Coast



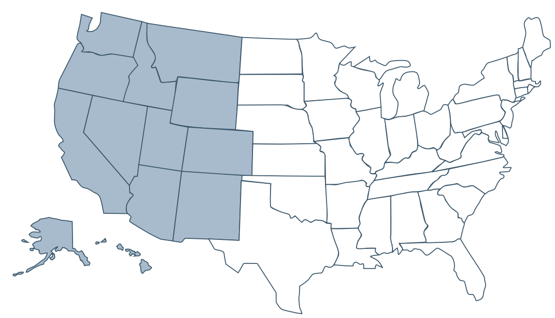
Midwest



Northeast



Southeast



West

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