

## Residential Mortgage Origination Channels

The purpose of this note is to provide some clarification regarding terminology surrounding different residential mortgage origination channels, as well as providing some estimates regarding shares of business across these different channels. In this note I review available data from a variety of sources. Our best estimate is that brokers are involved in about half of originations, although for subprime originations, the broker share is closer to 70 percent. Retail originations account for about 45 percent of originations, while direct marketing channels account for the remainder.

The largest mortgage companies in today's marketplace originate loans through loan officers at retail branches, through direct channels over the phone or internet, fund loans brought to them by mortgage brokers, and purchase closed loans originated by other, typically smaller lenders on a correspondent basis. Multi-channel lenders face the challenge of providing loans on a competitive basis to multiple different business partners: consumers who interact directly with the firm's loan officers, and mortgage brokers and correspondent lenders who typically interact with account executives.

Many smaller and mid-sized lenders also operate both retail and wholesale (broker and/or correspondent) channels. There is a great deal of fluidity between the broker and the correspondent roles played by small and mid-sized mortgage bankers. Some lenders may be an originator for certain core mortgage products, while brokering or acting as a correspondent lender for other products. In addition, when the origination market is strong, many brokers will access warehouse lines and expand their services to become full-fledged mortgage banking firms.

Historically, nonprime mortgage lenders relied to a greater extent on wholesale origination channels than prime lenders. Most nonprime lending was conducted by specialty finance companies; today, the largest lenders are typically involved in lending across the credit spectrum. It is not clear whether the higher broker share for subprime business will be sustained in a new environment where integrated financial services companies offer a wider variety of products to a more diverse group of borrowers. These companies certainly will use a broker channel to source originations, but will they use brokers to the same extent that subprime specialists did?

With this rich and dynamic set of origination channels and market segments it is quite difficult to consistently and accurately describe the share of loans that are originated through retail, broker, and correspondent channels. This difficulty accounts for some of the widely varying estimates that are frequently cited, e.g., for the share of mortgages accounted for by brokers. In the data analysis below, we examine a number of different sources to describe plausible ranges for these shares in today's market.

Table 1 provides data from recent editions of MBA's *Mortgage Originations Survey* (MOS) and *Subprime Mortgage Originations Survey* (SMOS). The MOS includes data from 114 participants, including the vast majority of the top 30 originators. In the second half of 2005, survey participants originated \$866 billion in first mortgages and \$189 billion in second mortgages. The SMOS is a new product with data only for the second half of 2005 at this point. This table shows that for the market as a whole in 2004 and 2005, 49-50 percent of loan originations were through a broker channel, 42-45 percent through retail originations, and the remainder through direct marketing channels. This tabulation excludes correspondent volumes from the survey participants. Inside Mortgage Finance estimates that correspondent

**Table 1: Channel Data from MBA's Mortgage Origination Surveys**

	2004-H2	2005-H1	2005-H2
<b>All loans (including subprime)</b>			
Retail	42%	44%	45%
Direct-Internet	3%	2%	2%
Direct-Other	4%	5%	3%
Broker	50%	49%	50%
<b>Subprime loans</b>			
Retail			27%
Direct-Internet			1%
Direct-Other			1%
Broker			71%

Source: MBA's Mortgage Origination Survey and Subprime Mortgage Originations Survey

**Table 2: Originations by Source**

	Based on Top 60 Originators			Allocating Correspondent Share 50% to Retail	
	Retail	Broker	Correspondent	Retail	Broker
1996	44%	22%	34%	61%	39%
1997	39%	26%	35%	56%	44%
1998	42%	28%	30%	57%	43%
1999	39%	26%	36%	56%	44%
2000	38%	28%	34%	55%	45%
2001	38%	29%	33%	55%	45%
2002	40%	31%	27%	54%	44%
2003	41%	28%	30%	56%	43%
2004	41%	31%	28%	55%	45%
2005	40%	31%	28%	54%	45%

Source: Inside Mortgage Finance, MBA calculations

production totaled \$920 billion in 2005, about 29 percent of their estimate of total production.

Table 2 which is based on data from Inside Mortgage Finance examines how shares across delivery channels have changed over time. Unfortunately, we do not have great data regarding whether correspondent business is more likely to be retail or broker. As a result, one must make an assumption regarding the mix of this business. In Table 2, examining data from the top 60 originators, we show the result of assuming that correspondent business is evenly split between retail and broker channels. This results in a broker share of 45 percent and a retail share of 54 percent.

Obviously, the true share could be anywhere between 0 and 100 percent. Some factors would indicate that the assumed 50 percent is too high. Running both a retail and a broker channel adds complexity to a business model, and the economic incentives to the broker might lead them to work directly with a large rather than a small lender. On the other hand, some factors would indicate that the assumed 50 percent is too low. The trends in consolidation show that larger lenders have more rapidly gained

market share in retail originations. Smaller lenders may have a comparative advantage in running a low overhead cost broker business. On net, we do not have a clear signal here regarding the broker and retail shares of small correspondent lenders. Additional data is needed.

Wholesale Access Mortgage Research and Consulting, Inc. annually conducted a study on wholesale lending trends. Their study showed that in 2005 participating lenders production was composed of 43 percent retail originations, 31 percent broker (“table-funded”), and 26 percent correspondent (“closed-loan”) business. Table 3 reproduces their numbers for the top 10 wholesale lenders. Note that while most of these lenders have both broker and correspondent channels, different lenders rely more heavily upon these different channels.

Over the past several years there has been an ongoing trend of consolidation on the origination side of the business. Table 4, utilizing data from Inside Mortgage Finance compiled in the Council to Shape Change (CTSC) report, shows that retail and correspondent channels have become concentrated to a greater extent among the top 15 lenders than the broker channel. In 2005, the top 15 lenders accounted for more than 80 percent of all retail originations, and almost 90 percent of all correspondent originations, but less than 67 percent of broker volumes. On the retail side, the substantial fixed costs of establishing a branch network provide economies of scale that benefit larger originators. Purchasers in the correspondent business are typically firms aggregating pools of loans for securitization, also a business that benefits from significant scale.

**Table 3: Wholesale Volume for 2005 by Production Channel (\$ Billions)**

Rank	Company	Broker	Correspondent
1	Countrywide Financial Corp.	103.3	233.2
2	Wells Fargo Home Mortgage	51.8	131.7
3	Washington Mutual	79.2	66.4
4	Chase Home Finance	50.4	14.1
5	CitiMortgage Inc.	13.7	44.8
6	Aurora Loan Services Inc.	12.7	38.8
7	Greenpoint Mortgage Funding	36.8	4.1
8	ABN AMRO Mortgage Group Inc.	28.8	11.8
8	Indymac Bank	28.1	12.5
10	Bank of America	26.5	0

Source: Wholesale Access Mortgage Research & Consulting Inc. as printed in Mortgage Banking magazine

**Table 4: Market Concentration by Origination Channel**

	1999	2005	Percentage Point Changes
<b>Retail</b>			
Top 5 share	28.5%	53.4%	24.9
Top 10 share	41.9%	70.7%	28.8
Top 15 share	49.8%	81.9%	32.1
<b>Broker</b>			
Top 5 share	24.2%	30.1%	5.9
Top 10 share	41.2%	51.9%	10.7
Top 15 share	51.6%	66.9%	15.3
<b>Correspondent</b>			
Top 5 share	31.3%	60.8%	29.5
Top 10 share	47.1%	79.9%	32.8
Top 15 share	55.2%	88.7%	33.5
<b>Servicing</b>			
Top 5 share	27.2%	43.3%	16.1
Top 10 share	40.7%	56.5%	15.8
Top 15 share	47.9%	62.1%	14.2

Source: *Inside Mortgage Finance, Council to Shape Change*

**Table 5: Summary of Channel Share Estimates**

	High	Low
Retail	54%	42%
Subprime loans		27%
Broker	50%	45%
Subprime loans		71%

**About Research DataNotes**

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What can we conclude? Table 5 summarizes the estimates presented in this note regarding the share of originations accounted for by retail and broker originations. The range of these estimates is due to differential sample coverage and varying assumptions regarding the likely composition of correspondent volumes. For the market as a whole, it seems likely that mortgage brokers are involved in about half of mortgage originations. This share is considerably higher for subprime loans. Market analysts should continue to track these shares given MBA's forecast that mortgage originations are due to decline to \$2.34 trillion in 2006 and \$2.41 trillion in 2007, and different segments of the market might fair better or worse in a period of declining total originations.

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