News Analysis

Reinsurance resurge

The CRT reinsurance market takes larger share of risk

Mortgage reinsurance through the ACIS and CIRT programmes is becoming an increasingly important part of the GSE CRT landscape as the capital markets programmes have suffered volatile market conditions in 2022, note onlookers.

When the GSEs unveiled CRT in 2013, the capital markets platforms (CAS for Fannie and STACR for Freddie) absorbed about 75% of the risk sold to the private sector while the reinsurance platforms (CIRT for Fannie and ACIS for Freddie) took the remaining 25%.

Over the last nine years the ratio has steadily become more balanced. In 2018, the GSEs sold $5.1bn in the reinsurance market and $14.25bn in the capital markets. In 2021, just over $14bn of risk was covered in the capital markets but almost $11bn was covered in the reinsurance market.

When comparing the RIF, or risk in force, the differential becomes even narrower. According to the CRT progress report, issued by the FHFA in Q4 2021, “In 2021, the Enterprises transferred risk on $1.1trn of UPB with a total RIF of $25bn. Securities issuances accounted for 57% of RIF, and reinsurance transactions accounted for 43% of RIF.”

Fannie Mae agrees that an increasing percentage of CRT risk will be placed in the reinsurance market. "We have revised our estimate for Connecticut Avenue Securities (CAS) issuance to a range of $13B - $15B for the year, down from the $15B projected at the start of the year. Some of the CAS volume is being shifted to our reinsurance program, Credit Insurance Risk Transfer (CIRT) given the recent volatility in credit

markets. Total single-family CRT issuance is expected to be approximately $20B in 2022," the GSE told SCI.

However, a Freddie Mac spokesman sticks to the official line and says, “We are due to do $25bn in CRT markets in 2022, and we expect a 70/30 split between STACR and ACIS.”

Pricing in CAS and STACR has widened sharply in line with most credit markets. Gathering inflation, the Fed moving to an aggressive hiking posture and the war in the Ukraine have pushed spreads wider. Significant supply and the promise of more to come haven't helped either, but to some extent the spread widening has been driven by factors unrelated to fundamental risk.

The reinsurance market has been far less affected by these external factors; investors remain focused upon underlying risk.

“Reinsurance markets have not widened as much as capital markets this year despite increased issuances, the Fed tightening, higher inflation and the Ukraine War. Reinsurers are buy and hold investors and pricing is largely driven by an informed view of risk. Unlike the capital markets that trade in the secondary market, reinsurance pricing is not driven by liquidity or mark-to-market accounting.” says Jeffrey Krohn, md and mortgage credit segment leader at Guy Carpenter.

Reflecting this immunity from non-risk based factors, ACIS pricing has remained stable. In the STACR markets, high LTV M-1 spreads have ballooned to around SOFR plus 370bp in Q1, compared to around plus 125bp in Q4 2021. ACIS spreads for the same tranche of risk have remained around plus 95bp, slightly narrower, in fact, than Q4 2021.

The same pattern is repeated throughout the capital stack. The STACR M-2 tranches have widened from plus 124bp to 276bp while ACIS M-2 tranches are still around plus 82bp. The STACR B-2 tranches have almost doubled from plus 160bp to plus 298bp while ACIS B-2 tranches are holding at plus 88bp.

Krohn further explains that collateral originated prior to the jump in interest rates are very attractive to the reinsurance market because of higher anticipated persistency and extended WALs. While capital markets will require higher spreads for increased WALs, reinsurers will generally take the view that their cumulative premium is greater, and thus, their upside to downside ratio has improved. This assumes underwriters take the view losses are unlikely to hit the laye*r*.

Average deal size in ACIS and CIRT has also increased. The average CIRT deal was just over $1bn in 2021 compared to $167m in 2015, while to date in 2022 the average ACIS transaction has been $820m compared to $295m in 2015.

Bond market choppiness has affected the mortgage insurance-linked note (MILN) market as well. Last year, there were 14 notes sold from the usual names like Arch, Essent,

Radian and MGIC. This year, however, there has been but two. Arch sold a $282m Bellemeade 2022-01 in January and MGIC sold a $474m Home Re 2022-01 in April.

A third is also believed to have been sold, which has not hit the tapes yet, but even so the run rate is well down on previous years. Those borrowers still maintaining a presence are said to be doing so simply so the market doesn't disappear.

By the end of April, yields for MILN tranches of 3% thickness had hit 9%, compared to 4.60% in January.

Other bond insurance providers are being drawn to the credit risk transfer reinsurance market rather than the MILN market thanks to its relative stability, note onlookers. In its Q1 earnings report, NMI reported that it has entered into a $290 million excess of loss reinsurance agreement with "a high-quality panel of third-party reinsurers, covering an existing portfolio of mortgage insurance policies written primarily from October 1, 2021 through March 31, 2022."

The credit risk transfer deal provides NMI with protection for aggregate losses on subject loans beginning at a 2.00% claim rate threshold and continuing up through a 6.75% aggregate detachment level.

At the end of March, Enact Mortgage Insurance Corporation, another mortgage insurance provider, announced it had secured approximately $325 million of additional excess of loss reinsurance coverage through a CRT deal with a panel of reinsurers.

Since 2015, Enact has executed approximately $4.4bn of CRT transactions, including approximately $2.6bn through the reinsurance market and $1.8bn through its Triangle Re MILN platform.

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