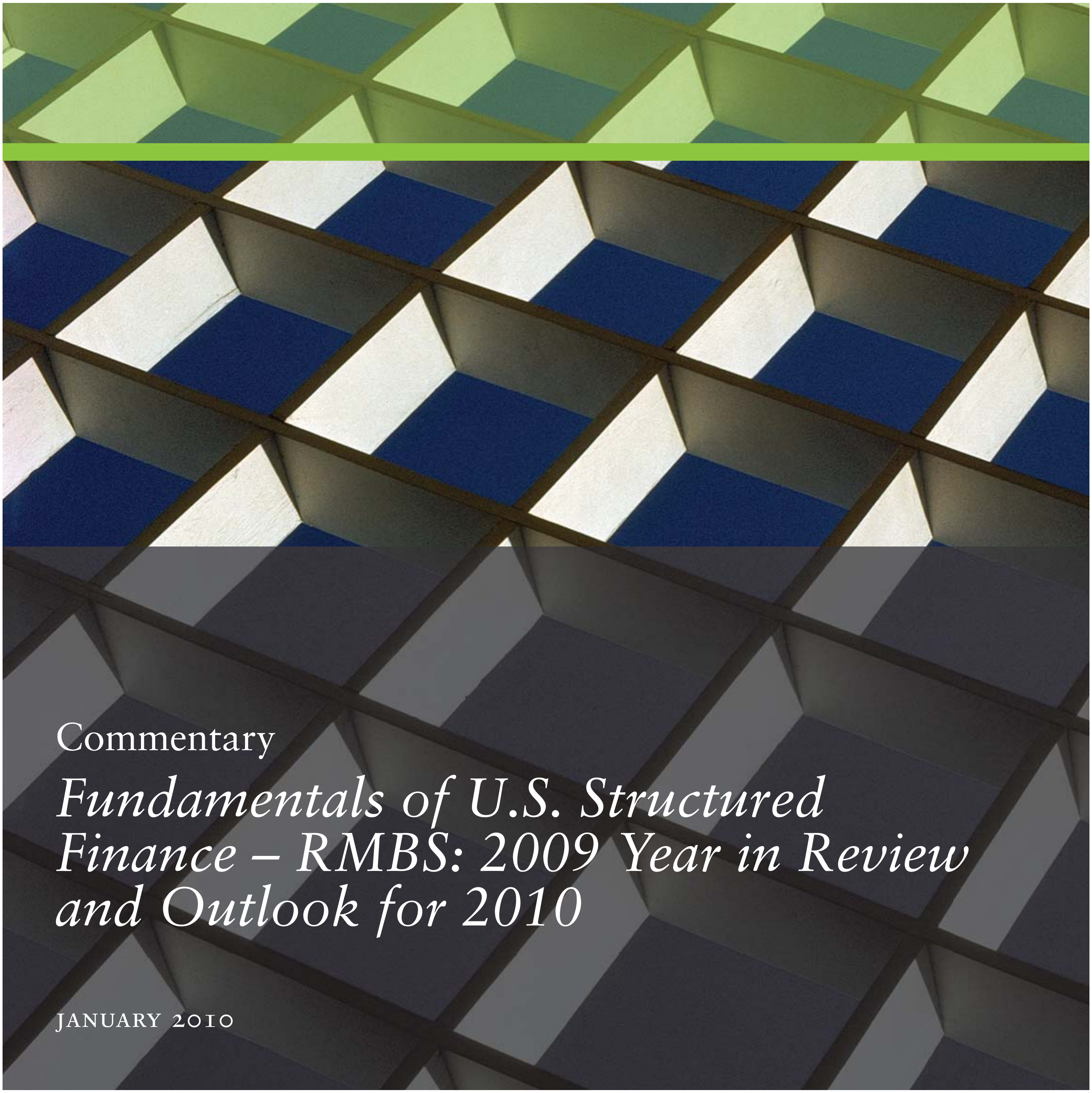

Commentary

Fundamentals of U.S. Structured Finance – RMBS: 2009 Year in Review and Outlook for 2010

January 2010

DBRS

Insight beyond the rating.

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Fundamentals of U.S. Structured Finance – RMBS: 2009 Year in Review and Outlook for 2010

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2009 Review and 2010 Outlook - U.S. RMBS

MARKET SNAPSHOT

2009 was a year of ReREMICs. There was a total of 124 ReREMICs[1] issued in the RMBS sector, representing a 75% increase from the previous year. Although core securitizations emerged in mid-year when Citigroup Mortgage Loan Trust 2009-A was rated by DBRS, they were greatly outnumbered by the ReREMIC volume. In addition, the market also completed five servicer advance securitizations last year after such transactions became eligible under the Federal Reserve's Treasury Term Asset-Backed Loan Facility program. Overall, ReREMICs dominated market issuance and accounted for approximately 90% of the total transactions that closed in 2009.

REREMICS

DBRS has noticed several trends in ReREMICs issued last year. The underlying collateral has evolved in 2009. Following heightened performance pressure in the prime sector, the collateral for ReREMICs has migrated from primarily Alt-A securities to a blend of Alt-A and prime bonds. Some "non-standard" collateral types such as non-front-pay seniors that are currently locked out from principal payments and subprime have also been issued on a limited basis.

ReREMIC capital structures have become simpler. Pro-rata pay or z-accrual structures common in 2008 and early 2009 are now largely obsolete. Plain sequential-pay structures (along with higher credit enhancement) also allowed investors to be comfortable accepting a rating lower than AAA for some ReREMICs. Many more ReREMICs issued in 2009 incorporated precautionary structural features in the form of exchangeable securities to protect against future potential rating volatility.

CORE (NON-REREMIC) SECURITIZATIONS

With respect to core securitizations in 2009, DBRS has rated a total of seven (six public and one private) transactions and provided credit assessments on two. All deals were backed by seasoned collateral ranging from 2 to 7 years. Pools were often positively selected to exclude any delinquent loans; however, many did contain mortgages that were modified to "current" from a previously delinquent status. Several of the transactions did not require servicers to advance any principal and interest payments on delinquent mortgages. The capital structures generally consisted of a plain-vanilla senior class and overcollateralization, and sometimes a mezzanine tranche. Principal was almost always paid sequentially to the senior class without any trigger mechanism.

DBRS considers numerous factors when evaluating a seasoned pool of mortgages including indexing property values to a projected housing trough, mapping full documentation loans to lower categories (higher penalties) due to weakened underwriting, and reverting loan status of a modified mortgage back to delinquent if it has not demonstrated a sufficiently improved payment pattern. Besides these credit considerations, DBRS also focuses heavily on representation and warranties, servicer evaluations and third party due diligence reviews. As a result, DBRS has on occasion requested due diligence samples to be expanded to 100% of the pool, if the initial reviews were not satisfactory.

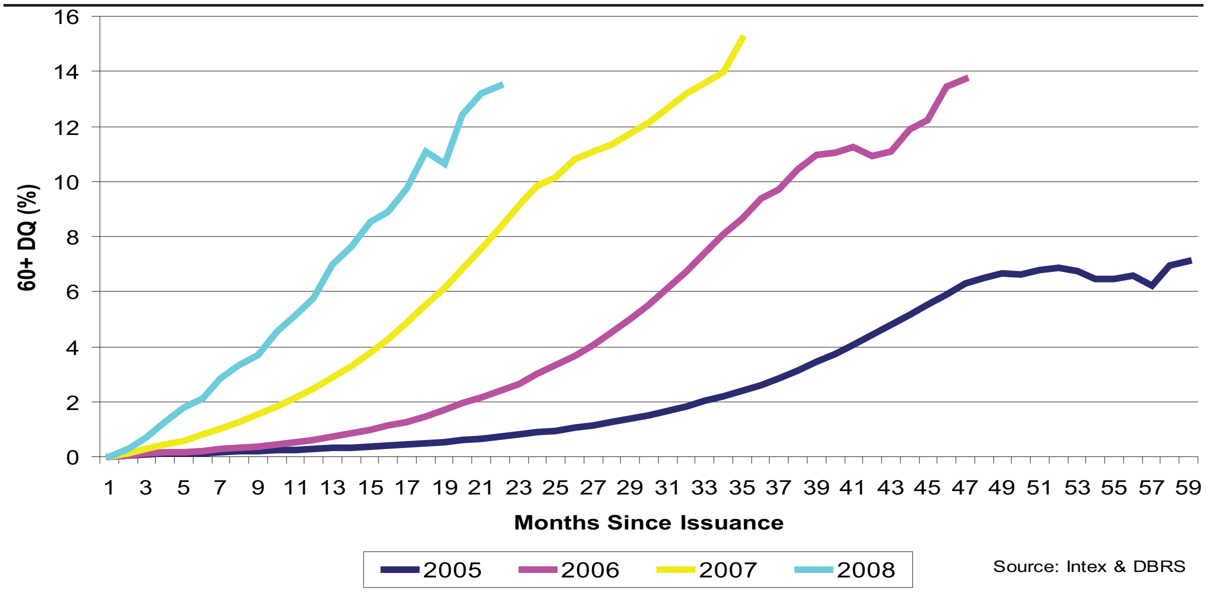
1. Source: Inside MBS & ABS, all %s are based on the number of transactions.

SECURITIZATION PERFORMANCE

Securitization performance, across all vintages, continues to be adversely affected by the declining home price appreciation (HPA) rates and the risk layering embedded in affordability products. In addition, a housing-induced economic recession and high unemployment rates further limited consumers' ability to make mortgage payments, and as such exacerbated bond performance.

In 2009, the performance deterioration was particularly alarming in the prime sector. On average, the serious delinquency rates[2] for the 2005 to 2008 prime vintages have risen 47% (weighted by the total outstanding balance of each vintage) from a year ago. As indicated in Chart 1 below, 2008 vintage delinquencies have nearly tripled since December 2008, and the remaining vintages have each exhibited a 66% (2007), 59% (2006) and 13% (2005) increase respectively.

Chart 1: Prime RMBS (2005 to 2008 vintages) - 60+ Days Delinquencies

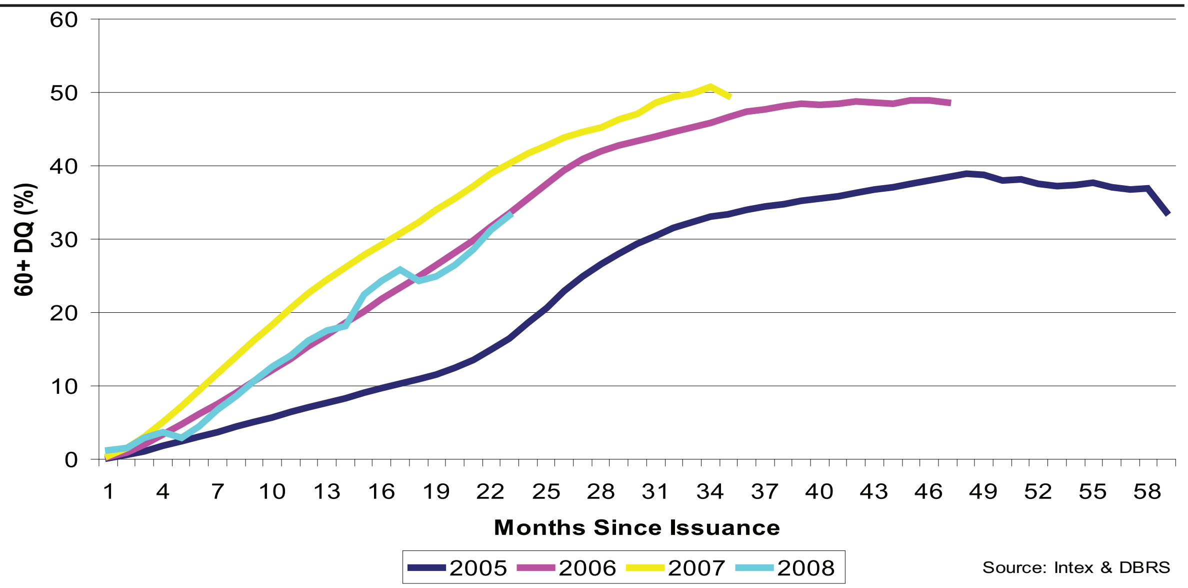


Source: Intex & DBRS

Despite the fact that prime mortgages still display the lowest overall defaults and expected losses, the rate of increase in prime delinquencies is, in fact, the most pronounced. For example, comparing the same period from December 2008 to December 2009, the subprime sector only experienced a 12% increase in serious delinquencies, as opposed to 47% for prime pools. Moreover, with the exception of 2008 and some 2007 transactions, subprime vintages seem to have generally reached the peak of their defaults and have exhibited signs of stabilization for the time being, as demonstrated in Chart 2 on the following page. The Alt-A sector, as expected, ended 2009 with a rate of increase in between the prime and the subprime sectors. On average, the serious delinquency rates increased by 19% in 2009. As shown in Chart 3 on the following page, some Alt-A vintage delinquencies started to flatten, albeit there were signs of a slight bump in the most recent three months.

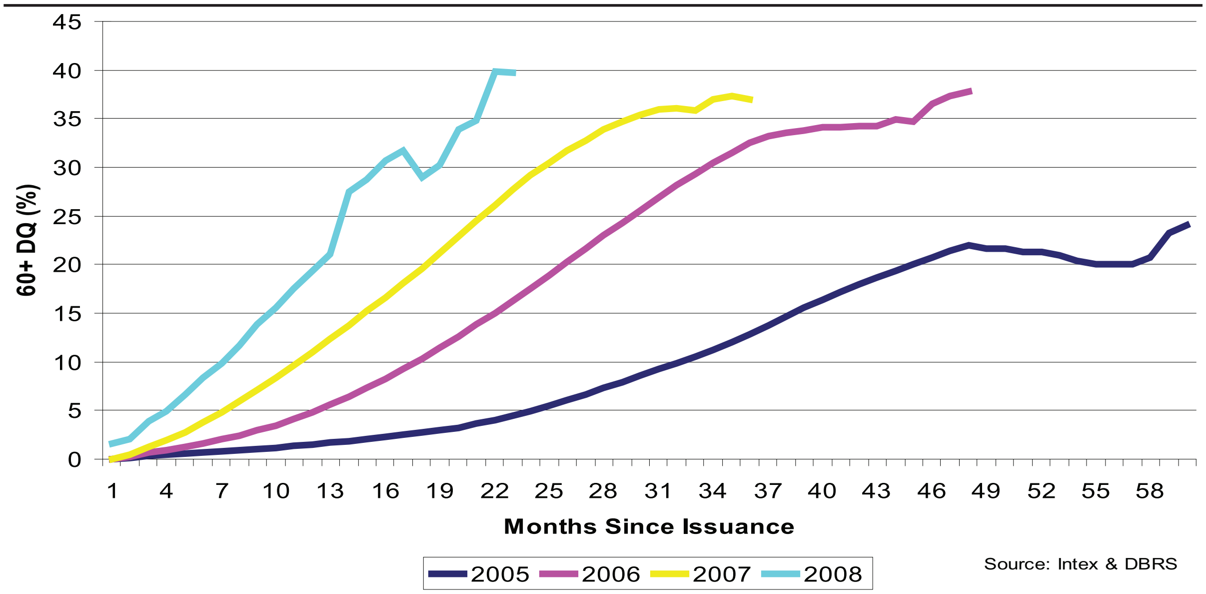
2. Serious delinquency: 60 or more days delinquent, including loans in bankruptcy, foreclosure and REO.

Chart 2: Subprime RMBS (2005 to 2008 vintages) - 60+ Days Delinquencies



Source: Intex & DBRS

Chart 3: Alt-A RMBS (2005 to 2008 vintages) - 60+ Days Delinquencies



Source: Intex & DBRS

TRANSACTION VOLUME OUTLOOK

DBRS projects a 10% to 20% increase in the number of RMBS deals in 2010. The ReREMIC trend will continue, but transaction volume will be volatile depending on the market prices of the underlying bonds. If prices remain competitive, issuers will most likely continue to expand the ReREMIC universe to include the "non-standard" collateral types such as non-front-pay seniors and subprime or even option ARMs. While most of these assets can be resecuritized, the resulting credit enhancement levels are often very conservative due to performance and cash flow concerns. In addition, as investors get more comfortable with the ReREMIC concept, some large-portfolio (as opposed to single-bond) ReREMICs may be executed as well.

There will also be a slight pick up in core securitizations, mostly backed by seasoned subprime or Alt-A collateral. Prime jumbo issuance will likely remain low, as the credit enhancement levels assigned by rating agencies do not currently represent a cost-effective exit strategy for issuers. Recent credit enhancements on prime jumbo pools are still very high, even on the cleanest pools, based on rating agencies' home price and other default assumptions. This is unlikely to change until the market starts to experience home price stabilization.

U.S. Mortgage Servicing Update

From a servicing perspective, as we look back on 2009, we will remember it as the year of regulatory reform, foreclosure moratoriums and modification mania. As we enter 2010, the U.S. government continues to introduce legislation aimed at preventing mortgage foreclosures and stimulating the housing market with incentives for loan modifications, short sales and deeds-in-lieu of foreclosure being offered to entice servicers and borrowers to work together as the market continues to experience record delinquencies.

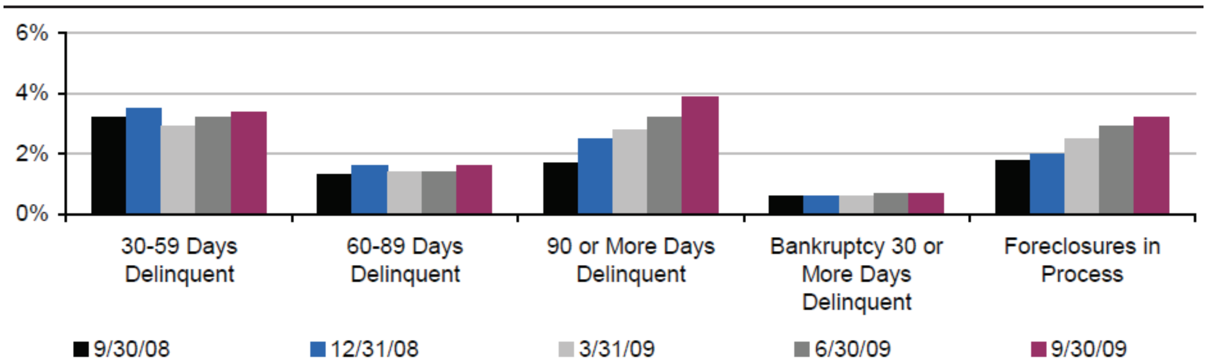
In this section, we discuss servicing trends, recent government initiatives and our expectations for 2010.

MORTGAGE PERFORMANCE

In December, the U.S. Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) jointly released their Mortgage Metrics Report[3] for the third quarter of 2009. The report provides performance data on first-lien residential mortgages serviced by national banks and federally regulated thrifts covering approximately 65% of all mortgages outstanding in the United States (about 34 million loans totaling $6 trillion in principal balances).

According to the report, mortgage performance continued to decline as a result of ongoing adverse economic conditions including rising unemployment and loss in home values. The percentage of current and performing mortgages fell to 87.2% of the servicing portfolio. Seriously delinquent mortgages— loans 60 or more days past due and loans to delinquent bankrupt borrowers—rose to 6.2% of the servicing portfolio. Foreclosures in process increased to 3.2%, while new foreclosure actions remained steady for the third consecutive quarter at 369,209. Of particular note, delinquencies among prime mortgages, the largest category of mortgages, continued to climb. The percentage of prime mortgages that were seriously delinquent in the third quarter was 3.6 %, up 19.6% from the second quarter and more than double the percentage of a year ago.

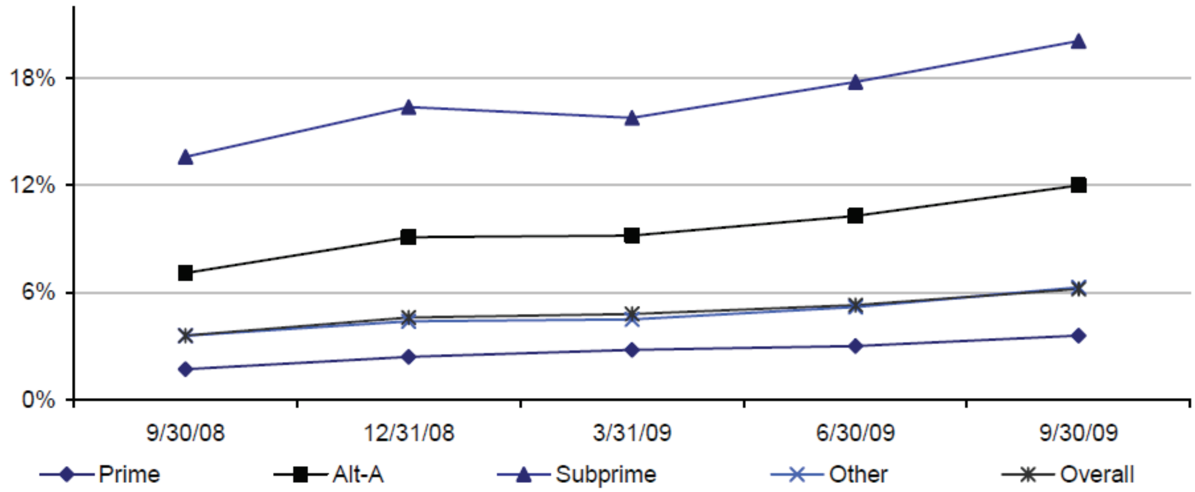
Overall Performance



Source: OCC and OTS Mortgage Metrics Report

3. http://www.ots.treas.gov/?p=PressReleases&ContentRecord_id=a3dc3ae9-1e0b-8562-eb2a-64c2fc422463

Percentage of Seriously Delinquent Mortgages:



Source: OCC and OTS Mortgage Metrics Report

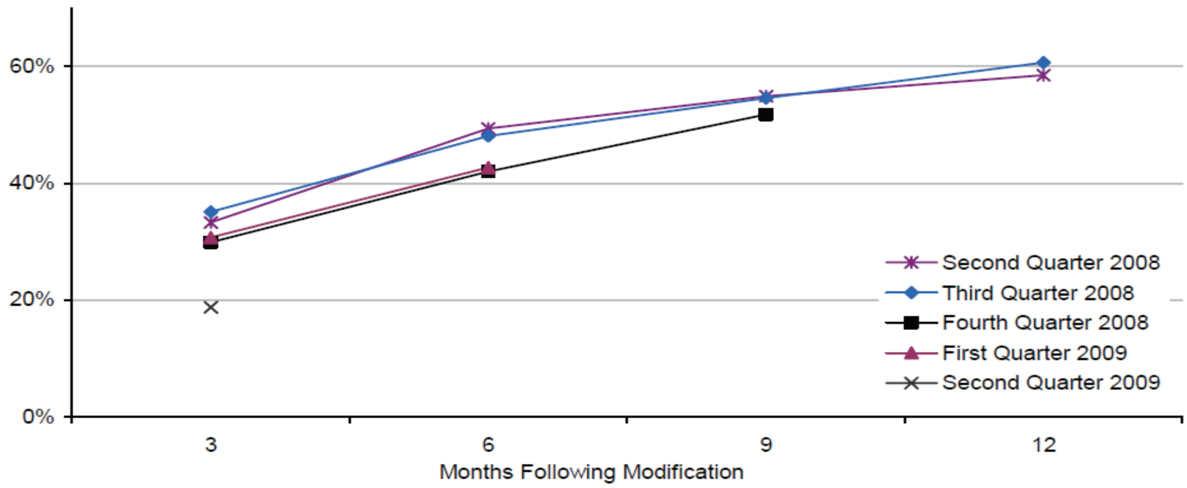
Modifications:

Large national banks and thrifts implemented more than 2.4 million loan modifications, trial period plans, or payment plans between January 1, 2008, and September 30, 2009, including actions taken under the Administration's "Home Affordable Modification Program" (HAMP). During third quarter 2009, servicers continued to increase home retention programs—loan modifications, trial period plans, and payment plans—to assist troubled homeowners and limit potential losses to banks and investors by avoiding preventable foreclosures. More specifically, servicers implemented 680,153 new home retention actions, up 68.7% from the previous quarter. The number of loan modifications declined for the second consecutive quarter as servicers emphasized the origination of trial period plans under HAMP and other proprietary servicer programs.

Servicers initiated 273,913 trial period plans under HAMP during the third quarter, for a total of 354,324 HAMP trial period plans from the announcement of the program in March through the end of September. In addition to HAMP actions, servicers implemented 121,314 trial period plans for their proprietary homeowner assistance programs, a 100 percent increase over the second quarter.

Despite growth in the number of modifications, modified loans continue to re-default at high rates. Measuring re-default as 60 or more days delinquent or in foreclosure, more than half of all modified loans re-defaulted within six months of modification.

60+ Re-Default Rate for 2008-2009 Modifications



Source: OCC and OTS Mortgage Metrics Report

Early indicators suggest more recent vintages with a higher percentage of modifications that reduce monthly payments are performing better than older vintages. More than 80% of all loan modifications implemented in the third quarter reduced monthly principal and interest payments for the borrower. Modified terms were primarily interest rate reductions and term extensions. Modifications with principal reductions increased to 13% of all modifications, up from 10% in the second quarter and 3% in the first quarter.

Type of Modification by Risk Category in the Third Quarter 2009:

	Prime	Alt-A	Subprime	Other	Overall
Capitalization	50.5%	57.5%	56.1%	63.0%	54.7%
Rate Reduction	83.8%	80.4%	79.9%	74.2%	81.1%
Rate Freeze	2.2%	2.9%	2.8%	1.5%	2.5%
Term Extension	47.6%	50.3%	45.6%	55.9%	48.0%
Principal Reduction	13.5%	15.8%	12.6%	5.7%	13.2%
Principal Deferment	4.4%	3.1%	1.1%	5.7%	3.1%
Unknown	2.9%	2.5%	2.2%	3.4%	2.6%

Source: OCC and OTS Mortgage Metrics Report

The 50% re-default rate on modifications continues to be staggering given the income verifications and trial modifications being done by most servicers. As a result, DBRS expects modifications that forgive mortgage debt will likely become the preferred loss mitigation strategy for many servicers during 2010. DBRS also believes that, similar to last year, we are going to see the U.S. government calling for large-scale loan modifications in 2010. DBRS will continue to monitor the industry for its use of modifications as well as its efforts to improve recidivism rates and minimize losses.

FORECLOSURE

A total of 3,957,643 foreclosure filings (default notices, scheduled foreclosure auctions and bank repossessions) were reported on 2,824,674 U.S. properties in 2009, a 21% increase in total properties from 2008 and a 120% increase in total properties from 2007 according to the RealtyTrac® year end report[4]. The report also shows that 2.21 percent of all U.S. housing units (one in 45) received at least one foreclosure filing during the year, up from 1.84% in 2008, 1.03% in 2007 and 0.58% in 2006. Four states accounted for more than 50% of the nation's 2009 total, with more than 1.4 million properties receiving a foreclosure filing in California, Florida, Arizona and Illinois combined. This was even with the majority of servicers issuing 90-day moratoriums on foreclosure filings and the government pushing servicers to modify delinquent loans.

In an effort to reduce foreclosures, DBRS expects modification programs will become even more prevalent in 2010, with debt forgiveness being offered more readily. The increased use of debt forgiveness may have a negative effect on some parts of the capital structure in deals. For example, this may cause the subordinate bonds to be written down prematurely or, if the losses are shared pro rata across the entire capital structure, the senior securities to take writedowns. DBRS will continue to monitor the industry for its use of modifications as a loss mitigation tool as well as the government's ability to implement incentive programs that will slow the pace of foreclosures.

TARP FUNDS REDIRECTED TO HELP UNEMPLOYED BORROWERS

The House recently passed a bill that would lend billions of dollars from the Troubled Asset Relief Program (TARP) to homeowners who are unemployed and delinquent on mortgage payments. The bill passed in December as an Amendment to H.R. 4173, the "Wall Street Reform and Consumer Protection Act." Under the proposal, $3 billion would be transferred from Treasury to the Department of Housing and Urban Development to make low-interest loans to homeowners who are at risk of losing their properties due to a job loss. The loans would be made to qualified borrowers and capped at $50,000. The bill also redirects $1 billion in TARP funds to help state and local governments buy and renovate foreclosed homes. The money for local governments is meant to help them buy and redevelop abandoned and foreclosed homes with an eye towards the development of affordable rental housing.

DBRS believes that throughout 2010 the country will see a lot more legislation introduced aimed at enhancing existing government programs and establishing new systematic plans to help struggling homeowners who are in default or facing foreclosure.

SHORT SALES

On May 14, 2009, the Obama Administration announced a Foreclosure Alternative Program (FAP) that provides incentives for servicers and borrowers to pursue short sales and deeds-in-lieu (DIL) of foreclosure in cases where a borrower meets the eligibility requirements for a Home Affordable Modification but does not qualify or is unable to keep up payments under a modification plan. The program is intended to allow families and servicers to avoid the costly foreclosure process and to minimize the negative impact of foreclosures on borrowers, financial institutions and communities. Listed below are some of the highlights of the program:

Foreclosure Alternative Program:

Borrowers will be eligible for the FAP if they meet the minimum eligibility criteria for a Home Affordable Modification but do not qualify for a modification or were unable to sustain payments under a trial period plan or a modification. Prior to proceeding with a foreclosure, participating servicers must evaluate each borrower to determine if a short sale is appropriate. In a short sale, a servicer allows the borrower to sell the property at its current value, even if the sale nets less than the total amount owed on the mortgage. Approval of a short sale requires the borrower to list and actively market the home at its fair value. The

4. http://www.realtytrac.com/contentmanagement/pressrelease.aspx?channelid=9&accnt=0&itemid=8333

sale must be an arms length market transaction with all proceeds (after selling costs) applied to the discounted mortgage payoff. If the borrower actively markets the property but is unable to sell it within the agreed upon time period, a servicer may consider a DIL. With a DIL, the borrower voluntarily transfers ownership of the property to the servicer, provided the title to the property is free and clear.

Minimum and Maximum Duration:

Under the program, servicers will allow borrowers at least 90 days to market and sell the property, with possibly more time based on local market conditions. The property must be listed with a licensed realtor experienced in selling properties in the neighborhood. Marketing of the property may run concurrently with the foreclosure process; however no foreclosure sale can take place during the marketing period as long as the borrower is acting in good faith to sell the property. There will be a maximum marketing period of one year for the property.

Incentive Payments:

Servicers receive incentive compensation of up to $1,000 for the completion of a short sale or DIL. Borrowers receive incentive compensation of up to $1,500 to assist with relocation expenses. The U.S. Treasury will share the cost of paying junior lien holders to release their claims, matching $1 for every $2 paid by the investors, up to a total contribution of $1,000 by Treasury.

In 2009, many servicers used short sales as one of their key methods of preventing delinquent loans from entering foreclosure. Several servicers also began using a form of "cash for keys" on their short sales in an effort to entice the borrower to help sell the home and leave it in "broom swept" condition with cash incentives far exceeding the maximum amount of $1,500 offered under the FAP program.

Short sales are typically pursued when the borrower is not able or willing to make payments on a modified loan and where it is clear that foreclosure would otherwise be inevitable. DBRS believes that, in this environment, using short sales as a loss mitigation tool is an effective way to get the home sold without having to incur the cost of foreclosure, preparing the home for sale, paying a realtor and maintaining the property (mowing the lawn, winterizing, etc.). As a result, DBRS expects short sales will be one of the key loss mitigation techniques used in 2010.

Completed Foreclosures and Other Home Forfeiture Actions:

	9/30/08	12/31/08	3/31/09	6/30/09	9/30/09	1Q %Change	1Y % Change
New Short Sales	13,549	16,809	18,619	25,128	30,766	22.4%	127.1%
New Deed-in-Lieu-of-Foreclosure Actions	842	1,186	1,298	1,120	1,233	10.1%	46.4%
Completed Foreclosures	127,730	94,928	90,686	105,993	118,603	11.9%	-7.1%
Total	142,121	112,923	110,603	132,241	150,602	13.9%	6.0%

Source: OCC and OTS Mortgage Metrics Report

REAL ESTATE OWNED (REO)

The current inventory level of 500,000 Real Estate Owned (REO) properties is expected to increase to roughly 1.2 million by 2012 according to a recent report released by J.P. Morgan[5]. Further, annual liquidation rates of REOs, foreclosures and short sales are expected to increase by 38% to 1.12 million in 2010 from the 810,000 in 2009. Consequently, with servicers' inventories at an all time high and timelines for REO sales lengthening, lenders continue to look for creative ways to dispose of these homes.

In January 2009, Fannie Mae announced that it would allow renters to remain in their homes even if their landlords enter foreclosure. This policy allowed renters living in foreclosed properties to sign a lease

5. J.P. Morgan Homebuilding report dated December 14, 2009.

with Fannie Mae while the property is up for sale. Then in November 2009, Fannie Mae introduced the Deed-for-Lease Program (D4L), a program designed to minimize family displacement, deterioration of neighborhoods caused by vandalism and theft to vacant homes, and the effect these have on families, communities and home price stabilization. D4L allowed qualifying borrowers of properties transferred through deed-in-lieu of foreclosure (DIL) to remain in their home and community by executing a lease of up to 12 months in conjunction with a DIL.

Even though, both of these programs were aimed at conforming balance servicers, DBRS expects that these types of programs will become more commonplace in the non-conforming residential mortgage market during 2010. Some non-conforming servicers have already been offering rent-to-own programs where the servicer rents the REO property to a potential buyer at an above-market rent. The renter (potential buyer) typically places 5% to 10% of the purchase price into a reserve account to lock in the option to buy. The difference between the actual market rent and the renter's monthly payment is added to the reserve account, which is used as a down payment on the property in one or two years.

DBRS believes that, while no servicer wants to be in the rental business, with current REO timelines averaging one to two years and the maintenance costs on these properties mounting (due to winterization, mowing the lawn, preventing vandalism, etc.), programs that allow the house to be occupied by someone who cares about how it is being maintained will likely increase the property value when it is ultimately sold. In addition, renting REO properties will help borrowers who are unable to get a mortgage in the current credit environment as well as offset future losses for security holders.

SERVICING FEES

There continues to be much debate in the industry regarding the adequacy of servicing fees given the current state of the market. Many servicers believe that a 50 basis point (bp) servicing fee is not enough to ensure the profitability of their operation for subprime and Alt-A product given the high delinquency rates and the increased use of modifications (which on average cost a servicer between $800 and $1,200 unless they are HAMP). Therefore, DBRS expects the trend of higher servicing fees and incentives for good performance to continue in 2010 given the high-touch nature of this type of servicing and the costs associated in complying with regulatory requirements and liquidating real estate owned (REO) properties.

Servicing fees vary by product and stage of delinquency but are currently ranging in the following areas:

- Prime: 20-25 bps
- Alt-A: 50-75 bps
- Subprime: 50-75 bps with incentives for successful workouts
- Special: 100-135 bps with incentives for successful workouts
- REO: 160 bps with incentives for low loss severities

SERVICER ADVANCES IN RMBS

In most U.S. Residential Mortgage-Backed Securities (RMBS), the servicer is required to advance delinquent principal and interest (P&I) to the trustee to the extent it is deemed recoverable. The servicer is also expected to make escrow advances for delinquent taxes and insurance (T&I) in addition to corporate advances for reasonable "out-of-pocket" expenses incurred by the servicer in the performance of its servicing obligations in connection with a default, delinquency, or other unanticipated event, including but not limited to, foreclosure proceedings and fees associated with the management and liquidation of any REO property (including legal fees).

Methods of reimbursement are specified in RMBS legal documents. Typically, servicers are reimbursed for advances in one of two ways: (1) monthly from general collections on the pool of mortgages (pool-level recovery) or (2) from subsequent collections on the related delinquent mortgage loan after it has been liquidated or when it reinstates (loan-level recovery). Though variations exist, P&I recoveries commonly are pool-level, while T&I and corporate are loan-level. Additionally, RMBS servicing agreements frequently specify that the servicer recovers any previously unreimbursed advances when a mortgage loan is modified, regardless of the specified reimbursement type.

Most RMBS transactions permit the servicer to be reimbursed for advances at the top of the trust payment waterfall. The speed at which servicer advances are reimbursed depends upon the type of advance and the foreclosure timeline in the jurisdiction where the related mortgaged property is located. For example, judicial advances are slower to collect through foreclosure than non-judicial advances; pool-level P&I advances are typically reimbursed much sooner than corporate and T&I advances which are reimbursed primarily through liquidation proceeds.

Presently, high delinquency rates and increased foreclosure and real estate owned (REO) timelines are causing liquidity challenges for many servicers that are advancing into RMBS. Loan-level recoveries on servicing advances can take several years. Additionally, the interest cost to carry relative to the servicer's credit facility can become a serious financial burden. Consequently, many issuers are weighing the benefit of advancing versus not advancing (P&I) in new RMBS transactions. While servicer advances are intended to provide timely cash flows and liquidity to a transaction, they do not serve as credit support. Further, deals where advancing occurs typically have higher loss severities than those that do not because the advanced interest will have to be reimbursed from the trust upon the liquidation of the mortgage. As a result, DBRS saw a growing number of transactions completed in 2009 where servicers were not required to advance any P&I payments. Since the lack of advancing did not affect the salability of the bonds DBRS expects this trend to continue into 2010 as the industry searches for ways to reduce the cost of securitization.

REPRESENTATION AND WARRANTIES

In 2009, as the industry continued to address the mounting delinquencies, the market increased its use of due diligence services to help identify representation and warranty (rep and warrant) violations in an effort to "put back" delinquent or fraudulent loans to sellers. Historically, repurchase demands were typically done within the first few months of a loan's origination and were for early payment defaults. Currently, mortgage originators are facing massive requests for repurchases on loans that are several years old for items such as fraud or improper lending practices. Since the loan limits for Fannie Mae and Freddie Mac increased, many loans that were once earmarked to be sold into private securities were instead sold to the government-sponsored enterprises (GSEs), which have much more liberal put-back provisions. Furthermore, bond insurers continue to experience financial pressure and are aggressively re-underwriting their portfolios in an effort to save some money.

With many lenders complaining that the pendulum had swung too far and it would be impossible for them to originate new loans when several years down the road they may be asked to repurchase a loan for minor issues the American Securitization Forum (ASF) worked with the industry to develop standard reps and warranties. Consequently, on January 13, 2010, DBRS published its expected standardized representations and warranties (and related covenant) for newly originated and seasoned mortgage collateral for residential mortgage-backed securitization (RMBS) transactions. The update provides expected standardized representations and warranties (and related covenant) for newly originated mortgage collateral, as well as a standardized set of representations and warranties for seasoned pools of mortgage collateral. The criteria update also clarifies the expected credit ratings of representation and warranty providers and related credit support. A copy of this methodology can be found at www.dbrs.com or by clicking here: Representations and Warranties Criteria for U.S. RMBS Transactions.

Conclusion

From an economic standpoint, 2010 will be a challenging year as the U.S. economy enters another year of stressful macroeconomic conditions. Delinquency trends will continue to rise due to sustained negative home equity, depressed home price forecasts, enduring unemployment, credit card reform and borrowers finding it difficult to refinance because of the tightened underwriting standards. As a result, DBRS expects to see an increase in personal bankruptcies in 2010. The level of bankruptcies may cause the subject of bankruptcy reform to resurface, particularly for legislation to close the loophole in the bankruptcy code that allows bankruptcy judges to modify the terms of mortgages on investment properties and vacation homes but not on primary residences. Currently, bankruptcy courts are unable to modify existing loan contracts for primary residences without express approval of the lender. Even though the "cram-down" legislation failed in 2009 many key senators still believe it would help the economy to have legislation that would allow judges to set new repayment terms for millions of mortgage holders who have ended up in bankruptcy court.

DBRS also believes that servicers will begin to be more aggressive in using principal-forgiveness modifications during 2010. To date, very few servicers have used a principal-reduction feature when modifying loans. However, as the U.S. government continues to pressure servicers to help distressed homeowners, drastic measures will need to be taken in order to improve the re-default rates for modified loans. To that end, discussions have already begun with the federal government to enhance existing modification programs to include incentives for debt forgiveness and second lien modifications in addition to issuing legislation that would relieve servicers of legal liability for utilizing these loss mitigation techniques on loans sold into securities.

For loans where the borrower is not able or willing to make payments on a modified loan and where it is clear that foreclosure would otherwise be inevitable, short sales will be the one of the most prevalent loss mitigation techniques used in 2010. A short sale allows the property to be sold by the borrower at an amount less than the full payoff on the loan. The servicer then releases the borrower from the lien. Servicers usually accept the reduced price in short sales to avoid all of the costs associated with foreclosing on the property and maintaining it as a real estate owned (REO) property. Short sales typically result in a loss severity that is approximately ten to 20 percentage points lower than that for REO liquidations DBRS believes that, in this environment, using short sales as a loss mitigation tool is an effective way to get the home sold without having to incur the cost of foreclosure, preparing the home for sale, paying a realtor and maintaining the property (mowing the lawn, winterizing, etc.).

DBRS will continue to monitor the servicing industry for trends with regard to the use of debt forgiveness as a loss mitigation tool as well as the administration's ability to help stabilize housing markets, improve the availability of credit and stimulate secondary market activity.

Insight beyond the rating.

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