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EC 630: Financial Economics

Research topic description

For my research topic, I will be writing about the to-be-announced (TBA) market for mortgage backed securities(MBS). I am basing my paper on the article *TBA Trading and Liquidity in the Agency MBS Market* by James Vickery and Joshua Wright. During the financial crisis of 2007-2009, mortgage securitization by private financial institutions declined to negligible levels. Agency mortgage backed securities continued to be issued, with the outstanding stock rising from \$3.99 trillion in 2007 to \$5.27 trillion in 2009. Agency MBS have the advantage that they carry either an explicit or implicit government credit guarantee, protecting investors from credit losses as a result of defaults on the underlying mortgages. 90% of trades of MBS are done on the TBA market, where the seller agrees to a sale price, but doesn't specify which particular securities will be delivered on settlement day. Instead, only the coupon rate, issuer, and approximate face value of the bonds is revealed ahead of time to the buyer. TBA prices, which are visible to market participants, serve as the basis for a variety of other MBS.

Vickery and Wright's article goes on to describe the features and mechanics of the TBA market and offer a review of then recent legislative changes to the market. I intend to follow up on the long term effects of the legislative changes, and research if there have been any other legislative changes to the TBA market, and what other effects those may have. The article also suggests that the liquidity benefits of TBA eligibility increases MBS prices and reduces mortgage interest rates. Given that mortgage interest rates have hit a 30 year high in recent months, I would like to test if the findings in the article still hold up with regards to the relationship between TBA eligibility, MBS prices and mortgage interest rates. I will use the Wharton Research Data Services for the data to perform my analysis.