QUARTERLY MARKET MONITOR

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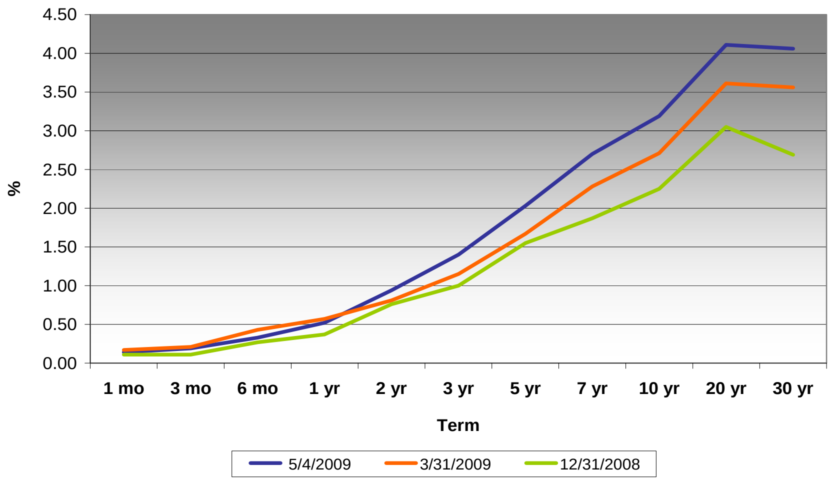
Market conditions improved modestly in the first quarter of 2009, but the economic environment remains challenging for OTS regulated institutions. The issuance of private-label mortgage securities, as well as the announcement of even more government assistance programs for asset-backed securities, suggest investors' appetite for credit risk has improved somewhat. However, the uncertainty about the treatment of legacy securities by these government programs and, perhaps overly optimistic expectations about the level of federal assistance by investors, resulted in greater spread volatility for commercial mortgage-backed securities. The U.S. economy continued to contract in the first quarter of 2009, and while consumer spending posted a slight increase, one-time factors that provided a boost to disposable income may not be enough to sustain the spending growth. Finally, the pace of home price depreciation decelerated in recent months as reported by various indices. Unfortunately, home sales continue to fall and delinquencies and foreclosures are rising. The result was the largest quarterly contraction in residential investment since the housing downturn began in 2006.

CAPITAL MARKETS

Conditions in the fixed income markets continued to improve with credit spreads narrowing and trade volume increasing for most investment grade products. The commercial mortgage-backed securities (CMBS) market exhibited the greatest level of spread volatility as the Federal Reserve announced an extension of its Term Asset-Backed Securities Loan Facility (TALF) to five years from three years beginning June 2009. Investors may now borrow funds at a higher rate for five years to purchase new senior securities backed by assets such as commercial loans. Initially, spreads for CMBS widened due to the market's disappointment that the program only addressed new issue CMBS (2009) and not the legacy securities. The omission of a program covering the legacy assets fueled speculation and uncertainty over the government's willingness to address the issue at all and, if so, whether the program be beneficial to market participants. As of May 5, 2009, investment grade CMBS spreads tightened to pre-announcement levels, as market participants now expect the creation of a government program to address the legacy securities. The various government programs have provided stabilization in specific market sectors. However, troubled markets that have not been addressed by federal programs are likely to be volatile until the degree of government assistance is known for that specific asset class.

The longer short-term rates remain low, the more likely that inflation fears will push long term rates higher. That is what we witnessed in the first quarter as the yield on the 10-year Treasury note rose more than 40 basis points while that of the 2-year was slightly higher (see Chart 1). As the Federal Reserve Board maintains a 0 to 25 basis point target fed funds rate, inflation hawks will continue to exhibit concerns in the form of higher long rates and a steep yield curve. The shape of the yield curve has been favorable for those that are willing and able to originate longer term loans as credit spreads remain near the wider end of the range while short-term rates are historically low.

TREASURY YIELD CURVE (CHART 1)



Source: U.S. Department of the Treasury

The issuance of agency MBS (FNMA, FHLMC, and GNMA) was strong in the first three months of 2009. The total volume of securities issued was more than $346 billion, a 62.4 percent jump from the fourth quarter of 2008, and a 6.9 percent gain from a year ago. The top three mortgage lenders in the country accounted for more than half of the issuance, according to Inside MBS & ABS.[1] Wells Fargo, Bank of America and Chase Home Finance accounted for more than 50 percent of the total market share of Agency MBS, with total volume of approximately $183 billion in the first quarter. Other producers included Flagstar Bank, Taylor, Bean and Whitaker, and GMAC Mortgage, which all posted an increase in issuance during the first three months of the year.

Re-REMICs dominated the new issue market in private-label securities. After a paltry year of production in 2008, with a total of only $58.4 billion for the year, a flurry of re-REMICs were issued in the early months of 2009 for a total of $5.3 billion in the first quarter[2] (see Chart 2). Re-REMICs allow for the creation of REMICs, with high credit ratings, backed by equal or lesser-rated securities from previous deals. The cash flows from the underlying securities are reallocated among the tranches to create new bonds with higher levels of credit enhancement and AAA ratings. All of the Re-REMICs issued year-to-date received an AAA rating from at least one credit rating agency. Market participants noted the improvement in residential mortgage-backed securities spreads aided by the announcement of the extension of TALF to include loans to any U.S. company that invests in securitized loans and legacy assets. This made issuance more attractive as the low cost of the collateral coupled with narrower spreads provided a greater economic incentive to create the securities. Investors in the re-REMICS include banks and insurance companies.

RE-REMICS AS A PERCENT OF NON-AGENCY ISSUANCE (CHART 2)

	Total Issuance (millions)	Re-REMIC/MBS (millions)	Re-REMICs % of Total
2003	586,216	7,747	1.32
2004	864,152	21,383	24.74
2005	1,191,310	16,786	1.41
2006	1,145,452	13,464	1.18
2007	707,013	25,483	3.59
2008	58,420	19,979	34.25
1Q 2009	5,305	5,305	100.00

Source: Inside MBS & ABS

ECONOMIC CONDITIONS

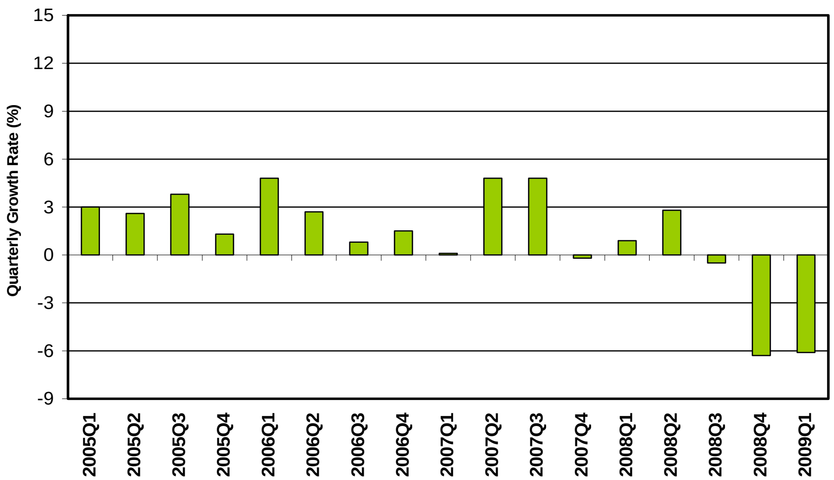
First quarter GDP posted a 6.1 percent drop following a 6.4 percent decline in the previous quarter (see Chart 3). The last two quarters taken

[1] Inside MBS & ABS, April 17, 2009.

[2] Ibid.

together (Q4 and Q1) were the worst back-to-back since 1958, when strike activity shut down the economy. Excluding 1958, this is the worst two-quarter period since at least 1947, which is when the U.S. began officially recording quarterly growth rates.

REAL GROSS DOMESTIC PRODUCT, AS OF 1Q 2009 (CHART 3)

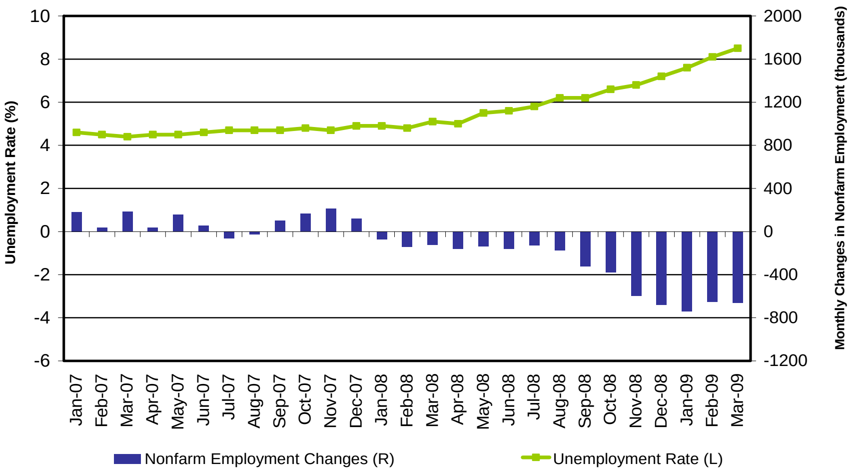


SOURCE: BUREAU OF ECONOMIC ANALYSIS

U.S. businesses lowered inventories by $104 billion, the largest decline in stockpiles since 1947. The inventory reductions cut Q1 GDP by 2.79 percent and suggest weaker demand for goods.

Despite the reduction in inventory, the consumer posted a slight rebound in spending, which rose by 2.2 percent (annualized) in the first quarter. After falling by 4.3 percent in the last three months of 2008 and 3.8 percent the previous quarter, January and February non-auto retail sales were boosted by a remarkable increase in disposable income and significant discounting. A 3.2 percent year-over-year increase in disposable income in the first quarter of the year fueled consumer spending. The gain is the first since October 2008 and is surprising amidst falling wages and rising unemployment. How can disposable (after-tax) income rise when the economy is losing 600,000 jobs a month, hours and bonuses are being cut, and fiscal policy measures to address financial turmoil are reducing interest and dividend payouts (see Chart 4)?

NONFARM EMPLOYMENT AND UNEMPLOYMENT RATE
AS OF MARCH 2009 (CHART 4)



SOURCE: BUREAU OF LABOR STATISTICS

The government extended a hand to households through a one-time cost of living adjustment to social security and other benefits, and a deep cut in personal tax payments in January 2009. Benefits rose by an annualized rate of 21 percent in cash value and tax payments were down 43 percent over the same period. Both of these transactions occurred in January 2009 when personal spending surged only to be followed by a sharp deceleration in February and March. The first quarter increase in spending was the first upturn since the second quarter of 2008.

However, equity prices were down 45 percent from their peak and housing prices continued to fall, which led to a sharp decline in household net worth. The net worth/income ratio fell from 6.3 in the first quarter of 2007 to 4.8 in the fourth quarter of 2008. Households also saved more, as evidenced by a 1 percent year-over-year increase in the first quarter savings rate to 4.2 percent. The one-time adjustments to benefits are not likely to sustain the increase in spending unless job losses abate and wages begin to rise.

Perhaps a more revealing view of demand can be gleaned from the trade data. Imports posted the biggest decline, 34 percent, since 1975, as businesses trimmed inventories in response to weaker consumer demand. Signs of the global recession were also evident in the 30 percent drop in U.S. exports, which when netted against the import decline, added roughly 2.0 percent of first quarter output as the trade deficit narrowed by $56 billion.

All investment sectors of the U.S. economy contracted in the first quarter 2009. Real business investment cratered by 38 percent (the largest quarterly decline since the 1940's), led by a 44 percent plunge in the purchase and leasing of structures and a 33.8 percent fall in outlays for equipment and software. The first quarter 2009 drop in capital expenditures was the fifth consecutive quarterly decline and the steepest to date.

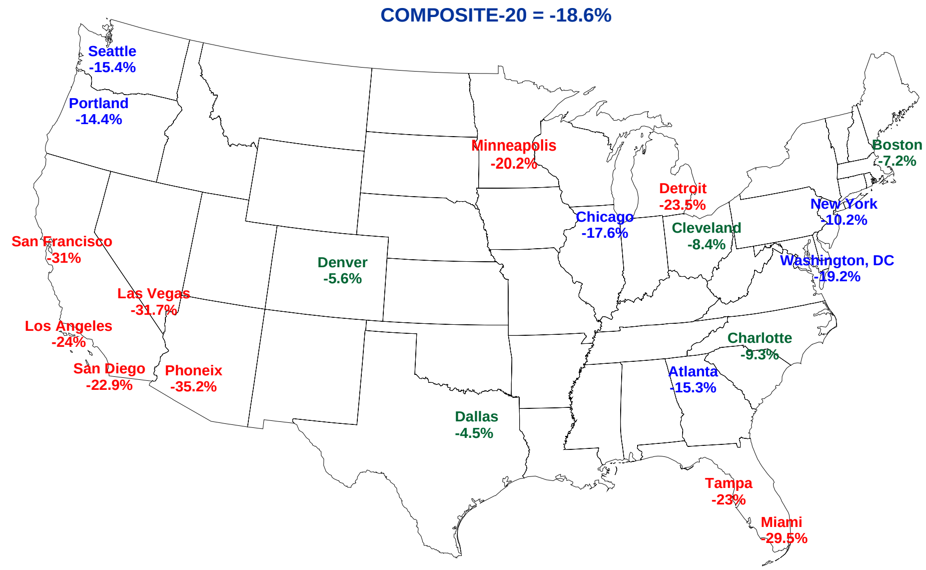
Housing conditions remained weak in the U.S. as reported by the 38 percent plunge in residential investment during the first three months of 2009, the worst quarter for housing since the downturn began in 2006. A protracted decline in homes sales led to a 49 percent year-over-year contraction in new home construction during the month of March in the United States. The first quarter was the worst for housing investment since the downturn began almost three years ago. Home sales continue to slow in both existing and new construction. The average price of a new home rose slightly to $258,000 in March 2009, while resale prices continued to fall during the same period. The supply of homes stands at roughly ten months, lower than the peak of eleven-plus months, but well above the equilibrium level of six months.

Government spending was also cut back by 3.9 percent, the largest reduction since 1995. Many of the reductions occurred at the state and local level where tax receipts fell and programs were minimized or eliminated.

HOME PRICES AND LOAN PERFORMANCE

The home price data offered some glimmer of hope that prices may stabilize. Some of the stabilization may be due to the foreclosure moratoria that just expired, which had the effect of reducing the supply of homes available for sale. Several indices reported some leveling of price depreciation. The FHFA monthly Home Price Index (HPI) increased by 1.0 percent in January and 0.7 percent in February. From a year ago, this index is down 6.5 percent.

MAP 1. CASE-SHILLER HOME PRICE INDEX: YOY CHANGE, AS OF FEB. 2009



SOURCE: S&P/CASE-SHILLER HOME PRICE INDICES

National median home prices, as reported by the National Association of Realtors, fell 11.5 percent in March from a year ago, an improvement over last month. The Case Shiller 20-city composite index showed an 18.6 percent drop in prices compared to a 19.0 percent year-over-year decline in the previous month. While the 20-city index continued to fall, February marks the first month since October 2007 that the index did not post a record decline. At February levels, average home prices are about where they were in the third quarter of 2003, but still down more than 30 percent from the peak in mid 2006.[3] Most cities recorded slower decreases in home prices from January to February with the exception of Cleveland, Charlotte, New York and Washington, D.C. The three worst performers with regard to home price depreciation in February remained the Sunbelt cities of Las Vegas and Phoenix in addition to San Francisco. It is too early to draw conclusions from the price indices as the impact of the foreclosure moratoria on price declines will likely manifest in the coming months. In addition, mortgage servicers are in the early stages of implementing the President's national loan modification program. The impact of this program on foreclosures is not likely to be evident for another two months.

As the government contemplates various policies to stem the rise in mortgage defaults, the delinquency and loss severity rates for residential loans continued to rise in February 2009. As shown in the attached charts 5-15, late payments on all types of mortgage loans rose albeit at a slower pace for subprime loans and ARMs. Nonetheless, subprime borrowers remain the worst performing with a serious delinquency rate[4] of 45 percent in February, a 0.5 percentage point increase from the previous month and the slowest monthly increase since August 2007. Option ARMs were the worst performing loan type, with a serious delinquency rate of 36.1 percent and like the subprime borrowers, exhibited a slight increase from the previous month. Other loan categories showed similar delinquency trends as the monthly increase rate is slowing, but still growing. Loss severity rates remain elevated and continued to rise. The highest rate remains that for subprime borrowers where the loss severity rate was 68.9 cents on the dollar. For the first time in several months, the deterioration in loan payment performance across all loan and borrower types has decelerated. Whether or not this is the beginning of an improvement remains to be seen.

[3] S&P/Case-Shiller Home Price Indices, published April 28, 2009.
[4] The serious delinquency rate is defined as percent of active loan dollar balances that are at least 60 days past due or in foreclosure/REO in a given month.

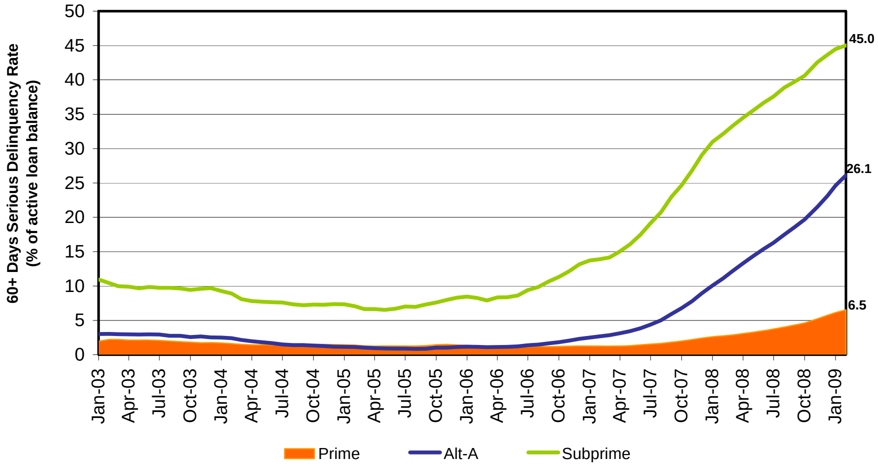
SUMMARY

The weak economy and difficult capital markets conditions continued to challenge thrift earnings. The persistent job losses and reduction in wages exerted considerable pressure on homeowners, especially those that struggled with higher monthly payments from rate adjustments. Lenders' efforts to restructure or modify loans were often thwarted by deteriorating financial conditions among borrowers who lost jobs or experienced a decline in income. The lack of demand for non-conforming loans by investors or other lenders caused originators to carry the loans in portfolio, thus reducing the amount of credit available to other qualified borrowers. Efforts to modify loans to reduce monthly payments may be more successful in stemming the growth in foreclosures. We will have a better idea of the effectiveness of the principal reduction modifications over the next few months. In the meantime, the deceleration in the growth of late payments and loss severity rates is encouraging, but rates remain at elevated levels and portend more losses.

The Re-REMICs revived the private-label MBS market. While issuance is minor compared to the entire MBS market, the ability for institutions to re-securitize lesser rated mortgage securities offers an additional source of liquidity to that market and potentially provides greater access to mortgage credit. Investors, which include financial institutions and insurance companies, appear to welcome the discounted price, higher yielding, credit enhanced structures, despite the 100 percent required risk weighting for capital purposes. The payment performance of the Re-REMICs will prove whether or not the issuers and credit rating agencies provided enough credit enhancements to maintain the original investment-grade ratings.

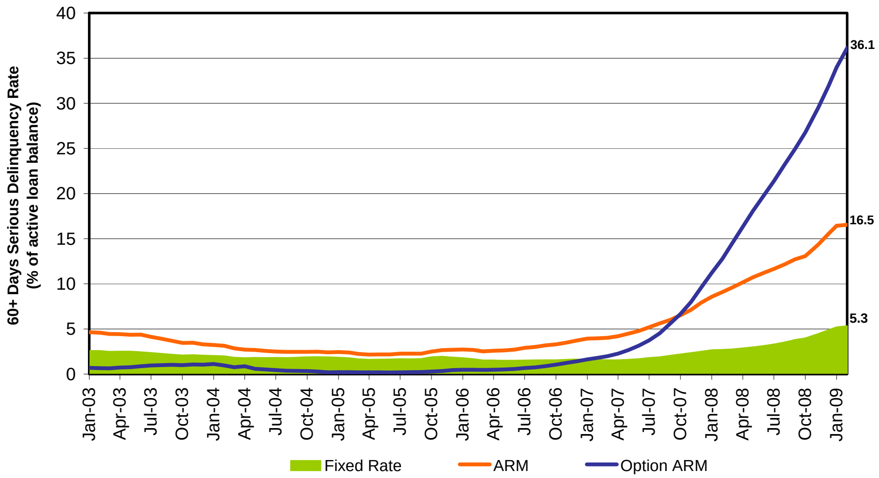
SERIOUS DELINQUENCY RATES BY INTEREST RATE & BORROWER TYPES

MORTGAGE LOAN PERFORMANCE BY BORROWER TYPE
AS OF FEBRUARY 2009 (CHART 5)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

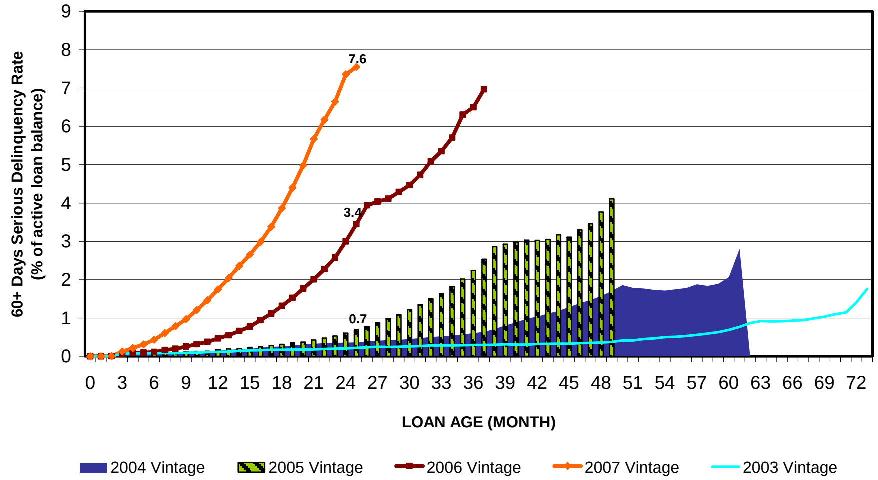
MORTGAGE LOAN PERFORMANCE BY PRODUCT TYPE
AS OF FEBRUARY 2009 (CHART 6)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

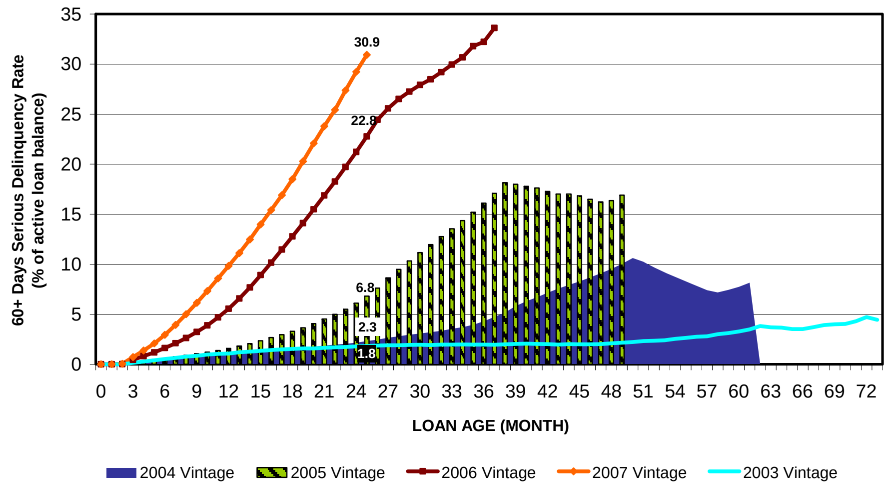
NATIONAL SERIOUS DELINQUENCY RATES BY VINTAGE

LOAN PERFORMANCE BY VINTAGE AND LOAN AGE: JUMBO
AS OF FEBRUARY 2009 (CHART 7)



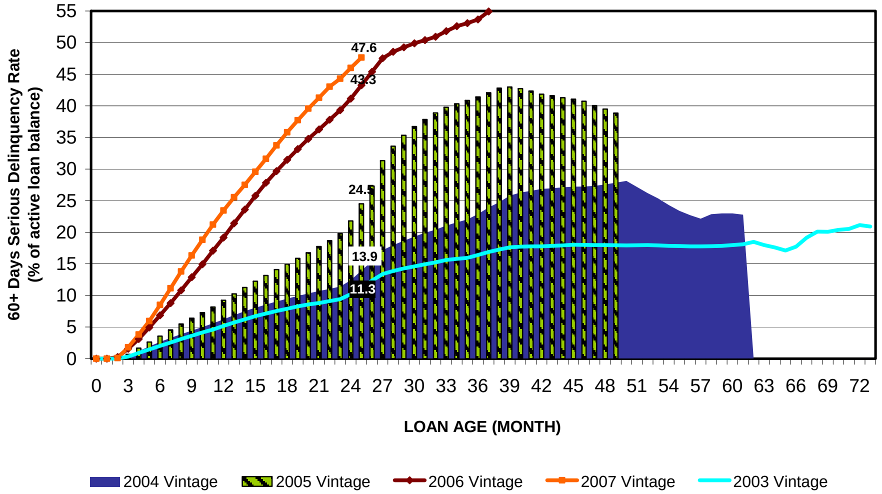
SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

LOAN PERFORMANCE BY VINTAGE AND LOAN AGE: ALT-A
AS OF FEBRUARY 2009 (CHART 8)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

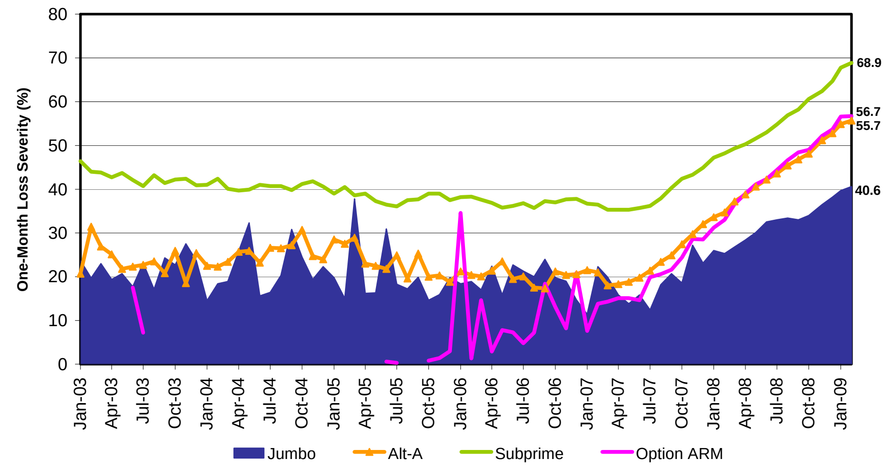
LOAN PERFORMANCE BY VINTAGE AND LOAN AGE: SUBPRIME
AS OF FEBRUARY 2009 (CHART 9)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

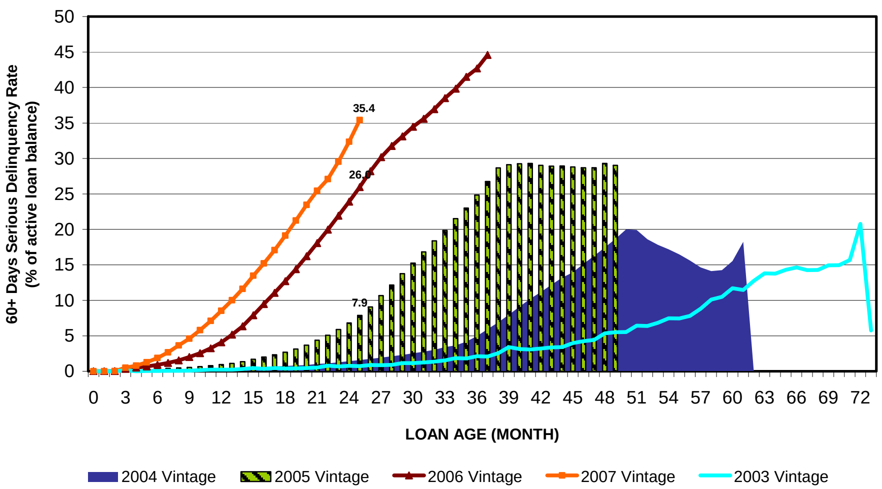
NATIONAL LOSS SEVERITY BY LOAN TYPE AND VINTAGE

LOSS SEVERITY BY LOAN TYPE, AS OF FEBRUARY 2009 (CHART 11)



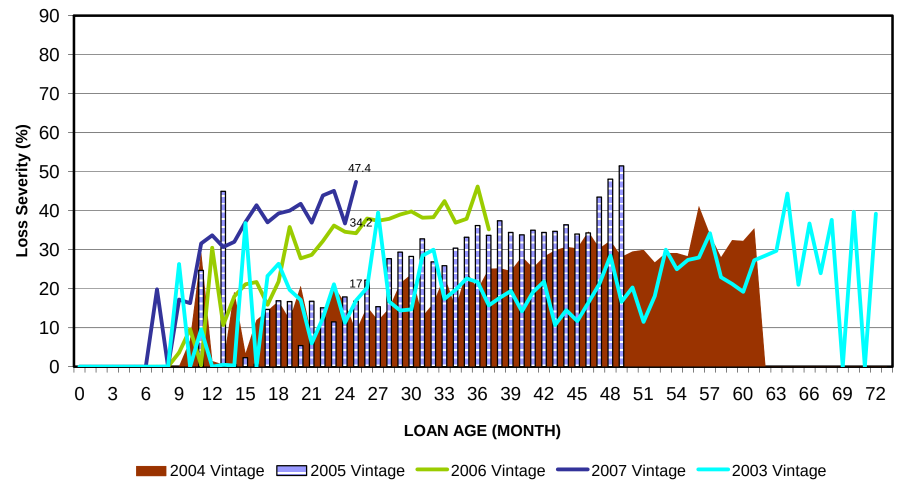
SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR
Footnote: Data for option ARM between Aug. 2003 and May 2005 are not available or have a value of zero.

LOAN PERFORMANCE BY VINTAGE AND LOAN AGE: OPTION ARM
AS OF FEBRUARY 2009 (CHART 10)



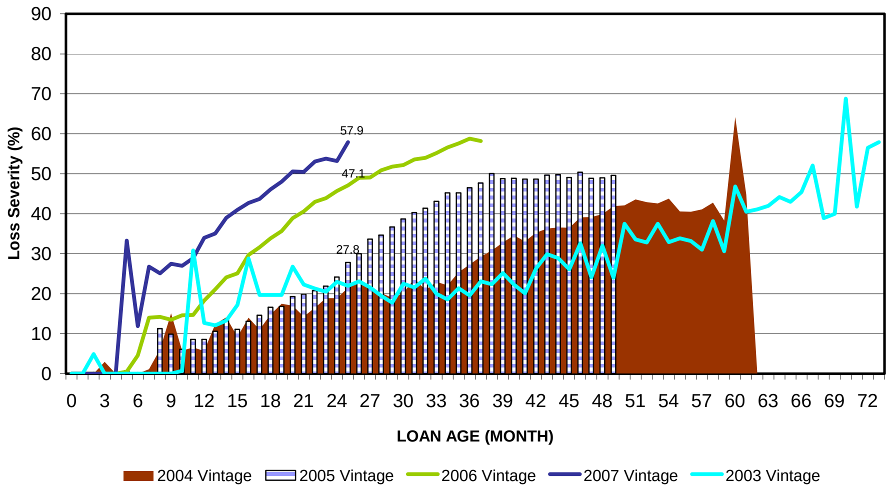
SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

LOSS SEVERITY BY VINTAGE AND LOAN AGE: JUMBO
AS OF FEBRUARY 2009 (CHART 12)



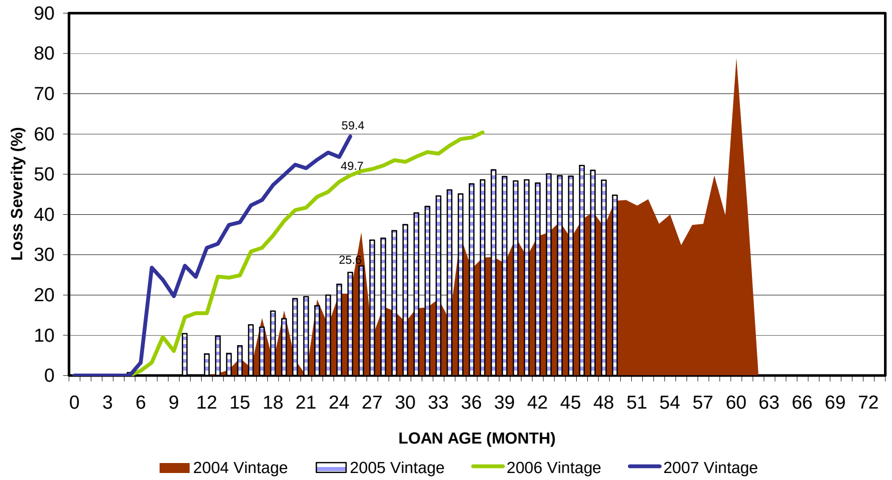
SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

LOSS SEVERITY BY VINTAGE AND LOAN AGE: ALT-A
AS OF FEBRUARY 2009 (CHART 13)



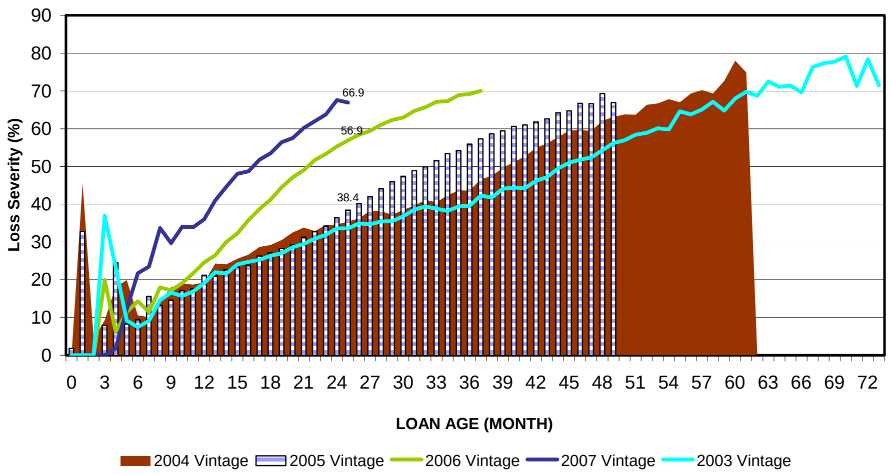
SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

LOSS SEVERITY BY VINTAGE AND LOAN AGE: OPTION ARM
AS OF FEBRUARY 2009 (CHART 15)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

LOSS SEVERITY BY VINTAGE AND LOAN AGE: SUBPRIME
AS OF FEBRUARY 2009 (CHART 14)



SOURCE: FIRST AMERICAN LOAN PERFORMANCE & CPR/CDR

SOURCES FOR CHARTS 5-15: FIRST AMERICAN LOAN PERFORMANCE AND CPR/CDR TECHNOLOGIES INC.

NOTE: DATA USES ACTIVE LOAN DOLLAR BALANCES OF FIRST LIENS ON A MONTHLY BASIS; DATA FOLLOWS THE MBA DEFINITION OF DELINQUENCY.

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