

The Role of Intermediaries During Boom and Bust

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Incentives in Lending



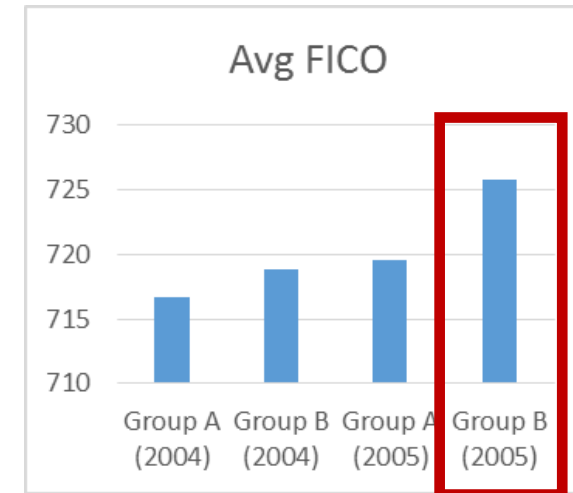
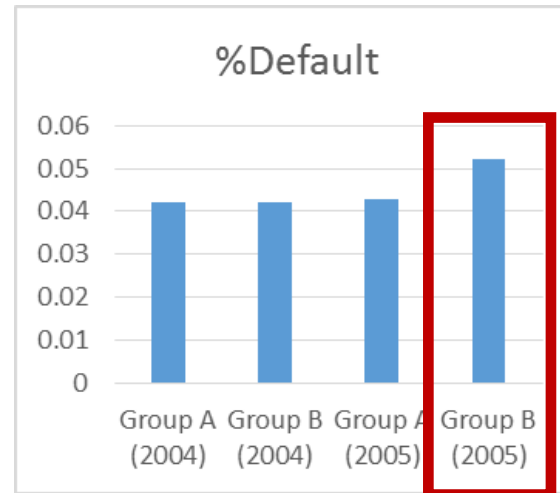
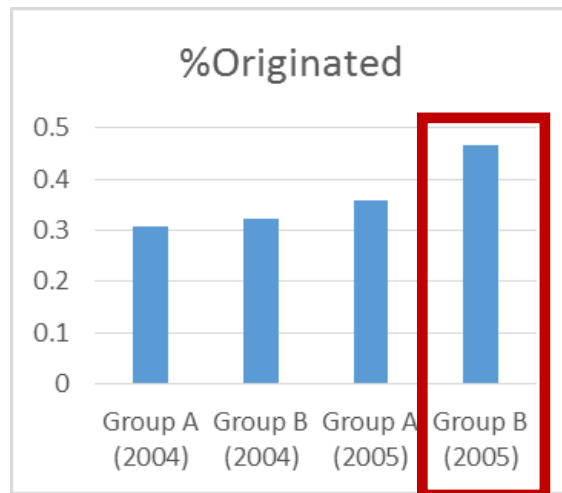
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Limiting High-Power Incentives

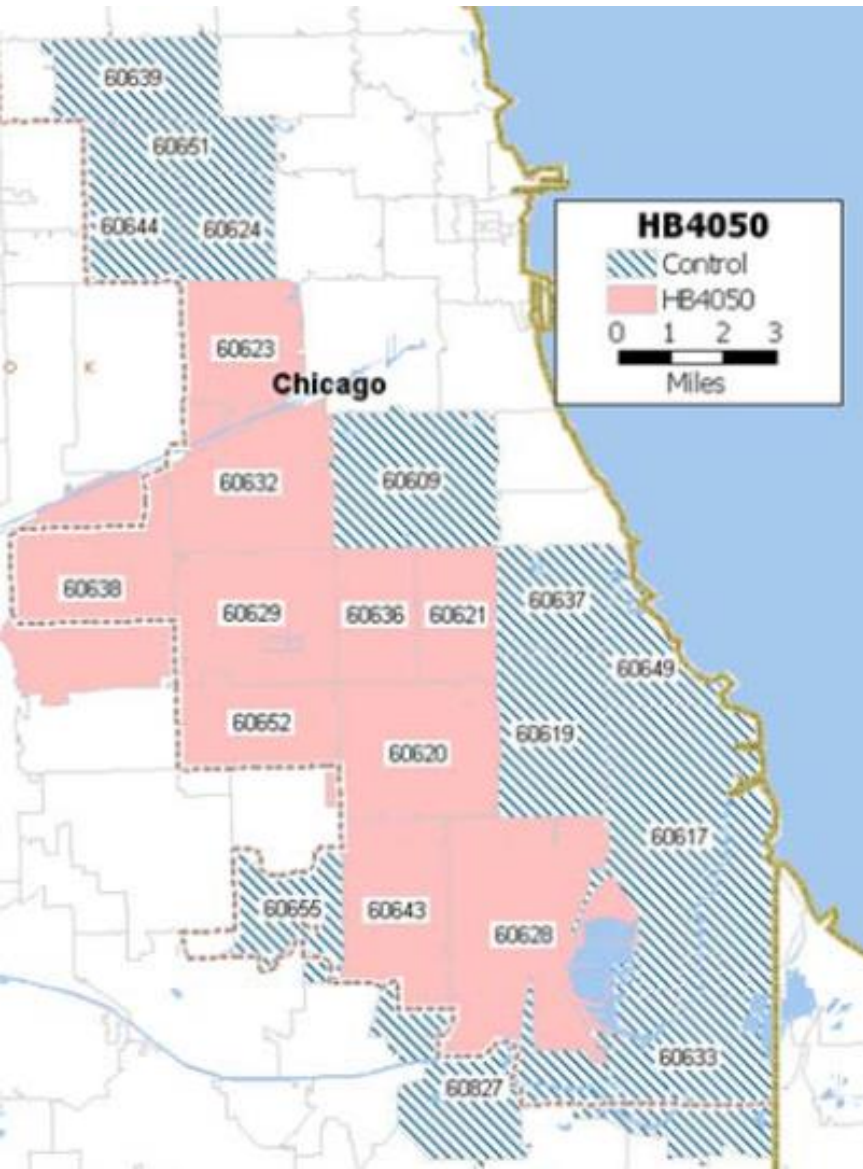
- **Loan officers:** Bonus-based compensation → poor mortgage quality



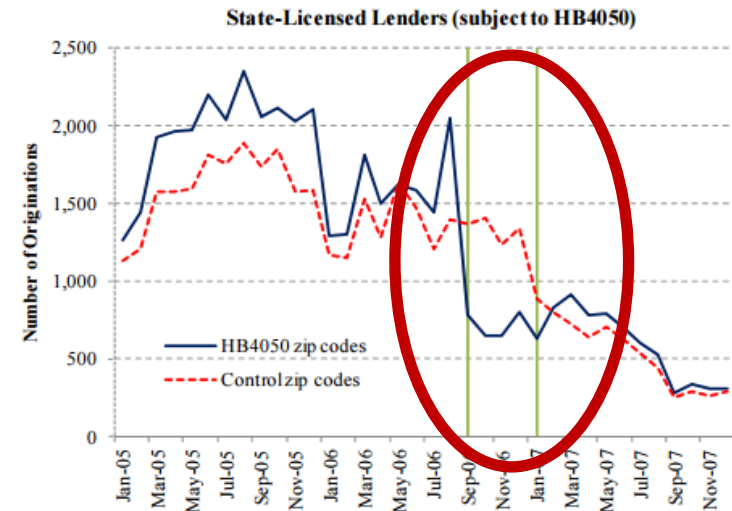
- **Appraisers:** Inflate valuations when under pressure
- Agarwal and Ben-David (WP); Agarwal, Ben-David, and Yao (MS 2015)



Anti-Predatory Laws Help, At a Cost



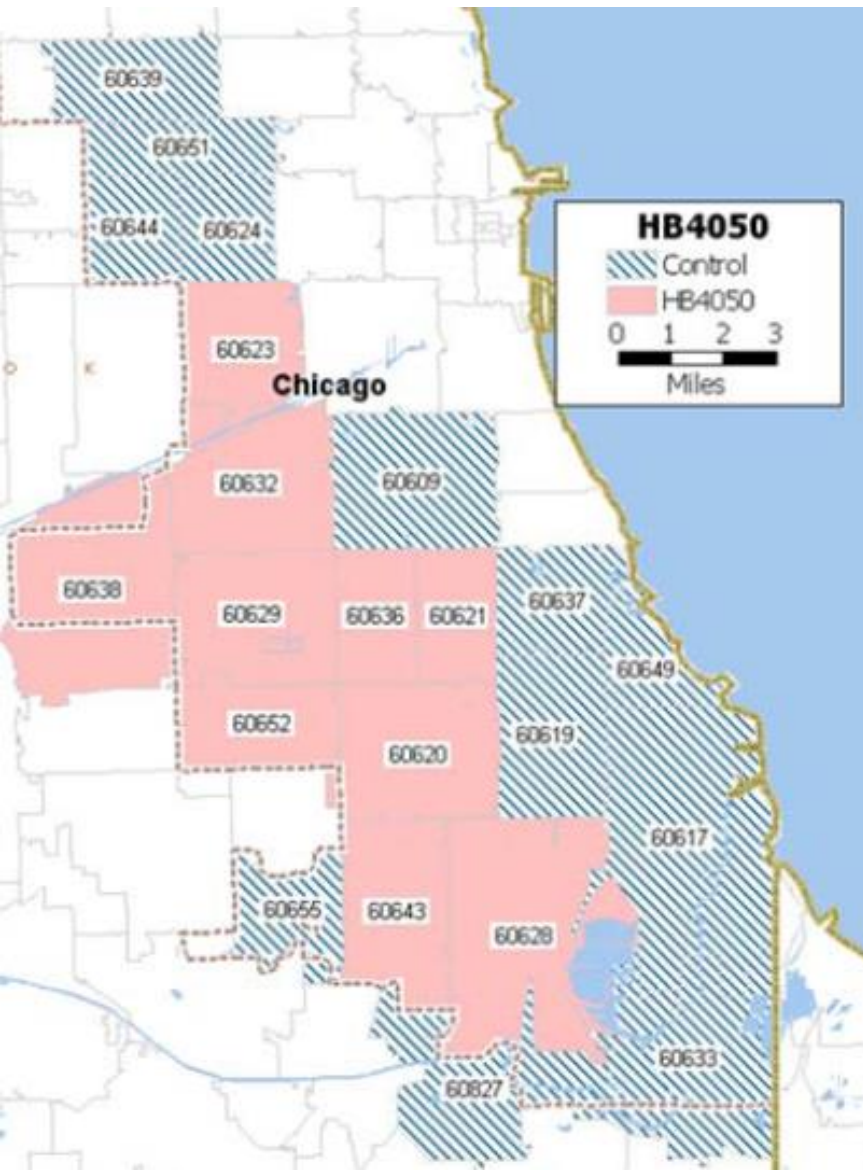
- Can deter predatory lending
- At the expense of lower market activity



- Reduced 18-months default rate: 27% → 21%
- Agarwal, Amromin, Ben-David, Chomsisengphet, and Evanoff (2014 JFE)

TY

Financial Literacy Has Little Value



- Borrowers not interested in mortgage counselling
- Mortgage counselling mandatory:
 - Did not change behavior
- Mortgage counselling conditional on product risk:
 - Changed behavior
- “Mortgage Risk Tax” would have worked just as well
- Agarwal, Amromin, Ben-David, Chomsisengphet, and Evanoff (WP)

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Incentives During Crisis



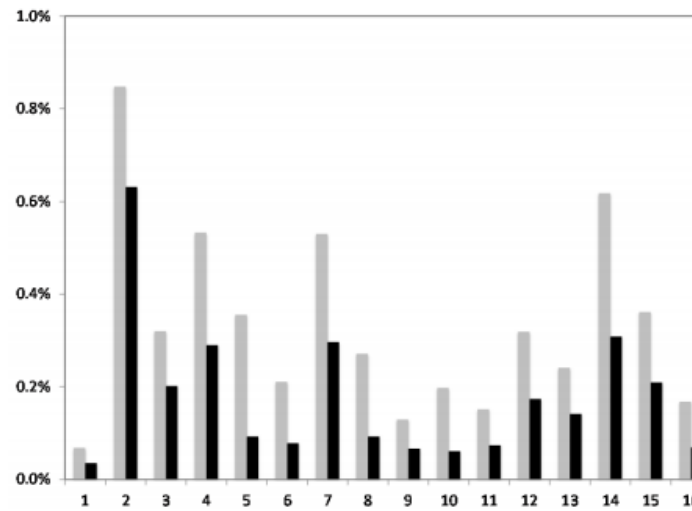
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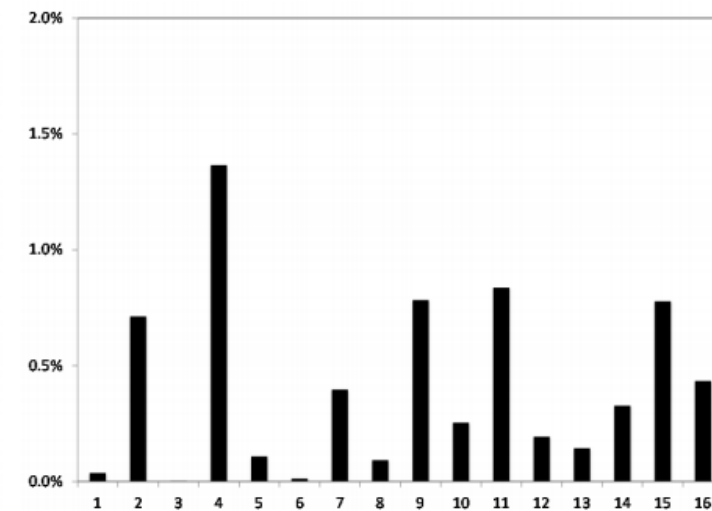
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Gov Intervention During Crisis Helps; Intermediaries Important

- HAMP: Government intervention is needed and can be effective
 - Renegotiations \uparrow
 - Foreclosures \downarrow
 - Consumption demand \uparrow
 - House prices \uparrow
- Strong servicer fixed effects



4(a): Trial (grey) and permanent (black) HAMP modification rates



4(b): Pre-HAMP permanent modification rates



- Agarwal, Amromin, Ben-David, Chomsisengphet, Piskorski, and Seru (2016 JPE)



Hold Up in Second Liens

	Ownership	Decision Making
First Lien	Securitized	Servicer A
Second Lien	Investor	Servicer B

	Ownership	Decision Making
First Lien	Securitized	Servicer A
Second Lien	Servicer A	Servicer A

- | | | |
|----------------------|---|---|
| |  |  |
| • Hold up incentives | | |
| • Action | Rapid | Delayed |
| • Resolution | Liquidate | Modify |
| • Liquidation | Foreclosures | Soft Liq |

- Agarwal, Amromin, Ben-David, Chomsisengphet, and Zhang (2014)



Conclusion

- Intermediaries have a crucial role in origination of mortgages and in loss mitigation
- During boom
 - Financial literacy and predatory lending
 - Aligning incentives of intermediaries
- During bust
 - Servicer incentives
 - Variation in servicer quality

