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Q2 2019 Impac Mortgage Holdings Inc Earnings Call

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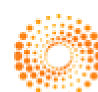

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PRESENTATION

Operator

Ladies and gentlemen, and welcome to the Impac Mortgage Holdings Second Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded. I would now like to turn the conference over to your host, Justin Moisio, our Chief Administrative Officer. You may go ahead.

Justin Moisio ***Impac Mortgage Holdings, Inc. - Chief Administrative Officer***

Good morning, everyone, and thank you for joining Impac Mortgage Holdings Second Quarter 2019 Earnings Call. During this call, we will make projections or other forward-looking statements in regards to, but not limited to, GAAP and taxable earnings, cash flows, interest rate risk and market risk exposure, mortgage production and general market conditions.

I would like to refer you to the business risk factors in our most recently filed Form 10-K under the Securities and Exchange Act of 1934. These documents contain and identify important factors that could cause the actual results to differ materially from those contained in our projections or forward-looking statements. This presentation, including outlook and any guidance, is effective as of the date given. We expressly disclaim any duty to update the information herein. I would like to get started by introducing George Mangiaracina, Chairman and CEO of Impac Mortgage Holdings.

George A. Mangiaracina ***Impac Mortgage Holdings, Inc. - Chairman & CEO***

Welcome, and thank you for joining Impac Mortgage Holdings Second Quarter 2019 Earnings Call. With me this morning are Brian Kuelbs, our CFO; Rian Furey our COO; Nima Vahdat, our General Counsel; Justin Moisio, our Chief Administrative Officer; Jon Gloeckner, Head of Financial Reporting; and Paul Licon, Chief Accounting Officer, will be available for the question-and-answer session.

For the second quarter of 2019, the company is pleased to announce GAAP earnings of approximately $4 million and core earnings of approximately $12 million. This marks the first reporting period since the third quarter of 2017, in which both of these measures of our financial performance have been positive and the first reporting period with a positive result in either metric since new management was fully installed in August of 2018.

Results from the second quarter of 2019 compare favorably to those from the second quarter of 2018 when the company posted GAAP losses of $97 million, primarily related to the write-down of goodwill and other intangibles and core losses of $6.7 million.

Without question, the story of the second quarter of 2019 is shaping up to be the story of the year, interest rates. More specifically, what appears to be the inexorable march to a 0 or negative rate environment in the United States. Several weeks ago, our good friend, Kevin Doyle, over at Cantor Fitzgerald, predicted we see 1.75% on the 10-year before we see 2.25%. This week, the 10-year briefly dropped below 1.60%, the lowest level since November 2016 with 1.50% seemingly to be within the market sights. We recall January of 2001 when the federal -- when the Fed embarked on a series of rate cuts that initiated a multi-year refinance wave. Origination volume, which was $1.1 trillion in 2000, doubled in 2001, and by 2003 approached $4 trillion. Volume remained at 2 to 3x of 2000 baseline until 2008.

Returning to 2019. Negative yielding corporate and government debt spiked over $15 trillion, more than 3x the level in October of 2018, primarily concentrated in the EU zone and Japan. That represents 1/4 of the global bond market. None of the $16 trillion in U.S. treasury debt has yet crossed into negative territory, but any one of a number of events could apply additional downward pressure in that

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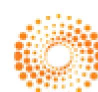

direction, Brexit, regional tensions, trade war escalation with tandem tariffs, currency devaluations and weakening global demand, also credit concerns over the non-investment-grade corporate debt market. In June, The Bank for International Settlements warned that a dramatic rise in borrowing in recent years by businesses with low credit profiles meant that $3 trillion of low-rated corporate debt, aided by a surge in CLO activity was becoming increasingly unstable. Most likely, lackluster GDP or market dislocation resulting from structural issues within the economy and/or geopolitical forces will elicit narrow conditions default response.

Coordinated monetary policy by the world central banks, rate cuts, quantitative easing and flight to safety and liquidity by investors via global capital flows. This fiscal policy is dead or it has simply been rendered irrelevant. By the end of June 2019, 10-year treasury rates declined 66 basis points from the beginning of the year to 2% in anticipation of easing by the Federal Reserve who accommodated with a 25 basis point reduction in its benchmark fund rate to 2% on July 31.

Mortgages outperformed treasuries for the first half of the year. Primary 30-year fixed-rate mortgage rates dropped 80 basis points from 4.50% at the beginning of the year to 3.75% at the end of June. 30-year fix rate now stands at 3.5%, equating to a payment savings for a borrower since beginning of the year of approximately $180 per month or $2,150 annually based on our annual conventional loan size of $310,000. Not surprisingly, the decline in interest rates drove industry-wide origination, specifically refinance volume. With respect to rate and term refinance activity, we estimate that 60% to 70% of outstanding 15- and 30-year fixed GSE product to be in the money, assuming a 25 basis point rate incentive, and we could argue that incent refi could be as low as 12.5 basis points. That's approximately $2.5 trillion to $3 trillion of GSE loans available from refinance.

Home equity will not be a constraint on rate and term refi activity to actually act as a catalyst to cash-out refi.

According to Black Knight, home price appreciation over the last several years has resulted in aggregate capable homeowners' equity of approximately $6 trillion as of the end of June, up from 2016 levels of $4.7 trillion. Tappable equity is the value of the home beyond the retained 20% equity that most lenders require of borrowers. The MBA Refinance Index just reached its highest level since November of 2016 refinance volume, up 112% from the prior year. While purchase volume is up only 7% since last year, the extraordinary refi activity has driven the total MBA Index to double its level from December 2018.

Sentiment has improved across the entire spectrum of mortgage participants. Fannie Mae's mortgage survey reporting a positive net profit margin outlook for mortgage lenders in the second quarter for the first time in nearly 3 years. And the MBA recently revised its origination volume forecast for 2019 to $1.75 trillion from $1.6 trillion.

With respect to housing, national home prices rose 3.4% annually in May, down slightly from 3.5% annual gain in April, according to S&P. According to the National Association of Realtors, existing home sales were stronger-than-expected in June, posted an increase of 2.8% over May. Existing national home sales for June were 1.6% higher than last year, the first annual gain in 17 months. However, the nation's higher-priced properties, especially in states, most impacted by the SALT deduction caps and interest rate deduction limitations associated with the Tax Reform Act of 2018, flashing signals of distress. According to Redfin, sales of homes listed at $2 million and above fell 16% in the first quarter of 2019, the sharpest decline since 2010. In our home market of Newport Beach, California, the average luxury sale price fell almost 22% year-over-year, Boston down 22%, Miami down 20%. It takes equal parts courage and coercion to go along the upper end of the housing market in those geographies and price points. But in general, the housing market appears stable.

In previous earnings calls, we've discussed the company's ability over market cycles to contract the scale, a consumer-direct center, call center, to calibrate to changing market conditions. While we have increasingly focused attention and resources on our NonQM franchise, we remain cognizant of our dual mandate to maintain optionality within the call center to quickly capitalize on GSE originations during low-rate environments. The ability to execute a material increase in volume in the second quarter validated our investment in a centralized scalable call center that competes favorably on streamlined process to deliver reliable and timely loan closings for our borrowers.

Specific to our origination results within our call center, the company produced $565 million in the second quarter of 2019 versus $320 million for the first quarter of 2019 and $459 million for the second quarter of 2018. We do not provide forward guidance on financial results, but we will note that the strength of the second quarter has carried over into the third. Originations from the call center at $365

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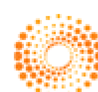

million in July versus $200 million for June and a forward pipeline projecting volume of approximately $500 million for August. I would like to remind listeners from our first quarter earnings call in May that our February volume from the call center was near $80 million. If all this volume materializes, the company will execute on more than a 6-fold increase in volume within 7 months. Our current staffing levels indicate call center capacity of upwards of $600 million a month, and we stand ready to lift that ceiling if market conditions remain favorable.

Refinance accounted for 90% of call center originations, 85% of refinance is purpose of cash out. Our NonQM business tends to be more rate and pricing elastic than our GSE business. In the second quarter of 2019, we produced approximately $75 million of NonQM from our call center versus $78 million in the second quarter of 2018. A third-party origination channel, or TPO, encompassing our wholesale and corresponding activities is the most significant contributor in our NonQM effort. We produced $240 million of NonQM from our TPO channel in the second quarter of 2019 compared to $228 million in the second quarter of '18. In total, across channels, NoNQM volume totaled $315 million in the second quarter of 2019.

As noted in our first earnings -- first quarter's earnings call, while aspirational, we believe our goal of an annualized run rate of NonQM of $1.75 billion to $2 billion by the fourth quarter of 2019 to be achievable. NonQM remains foundational to our business model and a core competency and differentiator for the company.

Since the company's founding in 1995, Impac has been recognized as a leader in providing loan products to borrowers in need of alternative credit to traditional Fannie Mae, Freddie Mac or government offerings. The design, origination, securitization and asset management of these products has been one of the core competencies of the company, having originated over $90 billion of such loans from 1995 to 2007.

Post-financial crisis, the company consciously maintained resources across these disciplines to manage our legacy Alt-A portfolio, in early 2014, extended that infrastructure as one of the first mortgage companies who anticipate and actively pursue the revival of NonQM market. We've originated $3.5 billion of NonQM since 2015, steadily, yet responsibly increasing our production from $130 million in 2015 to over $1.3 billion last year. We are rightly focused on monetizing the current opportunity within GSE origination to create gap in core earnings, drive growth of tangible book value, create liquidity to invest in our NonQM origination platform.

Rian Furey is now going to discuss some forms of this investment, detailing growth initiatives around the build-out of TPO correspondent, geographic expansion, product evolution and use of technology, all specific to NonQM. Rian?

Rian Furey ***Impac Mortgage Holdings, Inc. - President of Direct Lending & COO***

I

Thanks, George. As we discussed, the second quarter, it was one of exciting growth for our consumer direct channel. Volume spikes with consumers taking advantage of refinance rates that came down to levels we've not seen in the last 2 years. This slower rate trend, as you mentioned has continued into Q3 with near Brexit level rates available to customers today. For the last 6 quarters, we managed down the excess capacity in the channel while we spent into marketing and branding for new customer acquisition, and produced loans at better than normal margins in order to keep the optionality of the platform and allow for growth in the event of an eventual decrease in rates. Thanks to optionality, we're able to quickly bring back capacity to the platform by hiring experienced staff in the local market.

In addition, refinance volume, which has been concentrated in California and primarily expanding pretty eligible product is less complex to manufacture than our NonQM and government products, allowing us to operate more efficiently and get better turn times to our borrowers.

As excess capacity throughout the industry was absorbed almost overnight, margins on agency production returned to normalized levels. Our strategy in 2018 was to create liquidity by selling servicing rights held on our balance sheet. As a result of these servicing sales, we no longer service the majority of the loans that we've originated, and therefore, rely primarily on marketing, not repeat business or new customer acquisition.

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In Q2, our broad market advertising became increasingly effective, as low rate became a topic covered by the media, and as would be expected, we saw an increase in inbound traffic to our website and call center despite significantly reducing our marketing spend. Given many borrowers haven't refinanced in the last couple of years, but have had steady home price appreciation and the California's loans amounts are generally larger, borrowers can quickly recoup our $995 flat origination fee on a rate and term refinance or even just an 8th reduction in rate. Other borrowers are using additional equity from their homes to consolidate consumer debt or make home improvement. With the lower rate, we diversified our marketing messaging to include, again great benefit with called action in our TV, radio and online channel to supplement our existing NonQM-specific messaging creative. Demand for our NonQM offerings in the consumer direct channel has been consistent through the rate moves, but those transactions take longer to close and are currently outpaced by conforming refi.

In our third-party origination channel, we're still primarily focused on NoNQM production. In the second quarter, we saw a slight decline in dollar volume, but our unit count held strong. Our diversified geography out of California has, as expected, caused a gradual decrease in our average loan amount. We completed an overhaul of our lending guys in the second quarter, clarifying our products for our third-party originators, aligning slight differences that existed between our call center and TPO products and simplified pricing for our partners.

All those changes, we think, made our products easier to understand and originate, but will not materially change the creditworthiness of the assets we create. George?

George A. Mangiaracina ***Impac Mortgage Holdings, Inc. - Chairman & CEO***

Thank you, Rian. Continuing with the NonQM things. During the second quarter of 2019, the addressable market and securitized investor acceptance of NonQM continued to expand, reinforcing the company's commitment to this vision in business. Research by Nomura Securities projects $35 billion in origination volume in 2019 with $20 billion of securities issuance, both levels approximately double those for 2018. In a development that merits attention, on July 25th, the consumer finance protection bureau issued a notification of their intent to let the so-called qualified mortgage patch expire in January 2021. The QM patch confers qualified mortgage status on loans purchased or guaranteed by government-sponsored entities, even if those loans exceed 43% debt-to-income levels or do not adhere to other rigorous qualified mortgage requirements. In terms of addressable market, according to CoreLogic, 16% of all GSE loans originated in 2018 were done so with the QM patch, a total of $260 billion in loan volume. To provide context, the more securities predict that 2020's most aggressive theoretical estimate of NonQM market to be $100 billion. The company, through our NonQM franchise, welcomes and is positioned to benefit from proposals that would reduce the federal government's role in housing finance and drive an increasing share of that activity to the private sector.

Now I'm going to turn the call over to General Counsel, Nima Vahdat, to speak in more detail about recent CFPB developments related to the QM patch and GSE reform. Nima?

Nima Vahdat ***Impac Mortgage Holdings, Inc. - General Counsel***

Thank you, George. The concept of the qualified mortgage was introduced in 2010 with the passage of the Dodd-Frank act. QM and ability to repay regulations were subsequently issued by the CFPB and the rule took effect in January 2014. QM loans were designed to give lenders a safe harbor, improving the consumers' ability to repay their loan. When the QM and ability-to-repay rules first became effective, there was a limited secondary market available to purchase loans, which would otherwise be NonQM. Even if there were such a market, the legal risk associated with NonQM lending was perceived to be higher due to the lack of a safe harbor, leaving many lenders reluctant to enter the space to this day.

As a result, the CFPB included the QM patch in their rules to give lenders a bridge until the secondary market for NonQM emerged. Without this bridge, many of the QM restrictions, in particular, the DTI limitation, with a severely depressed lending in retirement home values in the mortgage market, generally, were already stagnant. Fast forward 5 years, and we're at a stage where the CFPB has come to look at the QM patch as a crush to the industry and not a bridge. The CFPB never intended the patch to be used so heavily, and it's likely that they didn't think that the GSEs would be so heavily involved in the secondary market this long after the crisis.

Providing this advanced notice of rule expiration puts the industry on notice to prepare themselves with other loan products or secondary

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market outlooks for loans that would have otherwise been GSE-eligible. Even if some of these borrowers shift to FHA or VA loans, the CFPB acknowledges the impact of this change on the industry as nearly 1 million mortgage loans made in 2018 would not have met the general QM test.

That said, there could be changes to the CFPB approach between now and 2021. The CFPB may elect to delay the expiration of the patch, they may elect to raise the DTI limit to include more loans on a QM definition or some have suggested that it might actually make sense to reduce the DTI limit or add a residual income requirement. What is without question is that the CFPB and likely the current administration is looking to reduce the industry's reliance on the GSEs without GSE reform or taking the GSEs out of conservatorship.

With over 5 years of NonQM expertise plus crisis and nearly 25 years of experience in the alternative credit space, Impac is uniquely positioned to take advantage of this market increase. To give some perspective, 33% of Impac's funded loans in 2018 had a DTI exceeding 43%. This is a function of Impac's focus on NonQM lending. With Impac's existing stable of secondary market relationships, originating more loans for sale to these non-GSE outlets is a natural extension of Impac's existing business.

With that, I will now turn the call over to Brian Kuelbs to review our financial results.

Brian P. Kuelbs ***Impac Mortgage Holdings, Inc. - Executive VP & CFO***

Thank you, Nima. I'll now provide a brief review of the financial results for the second quarter. We reported net earnings of $3.9 million or $0.18 per diluted common share in Q2 of 2019 compared to a net loss of $97.4 million or $4.65 per diluted common share in Q2 of 2018.

Core earnings were $11.9 million for Q2 of 2019 or $0.56 per diluted common share as compared to a loss of $11.4 million or $0.54 per diluted common share in Q2 of 2018.

For the 6 months ended June 30, 2019, we reported a net loss of $8.7 million or $0.41 per diluted common share as compared to a net loss of $93.5 million or $4.46 per diluted common share for the 6 months ended June 30, 2018.

Core earnings for the 6 months ended June 30, 2019, were $6.1 million or $0.29 per diluted common share as compared to a loss of $21.3 million or $1.02 per diluted common share for the 6 months ended June 30, 2018.

I'll now address revenue and originations. Gain on sale increased to $30 million for the second quarter of 2019 compared to $19 million for the second quarter of 2018. For the 6-month period ending June 30th in 2019, gain on sale increased to $42 million compared to $40 million for the comparable period in 2018.

With regard to volume during the second quarter of 2019, total origination volume was $821 million. This was a decrease of 21% from about $1 billion in the second quarter of 2018.

Regarding loan purpose. During the second quarter of 2019, refinance volume decreased approximately 5% to $626 million as compared to $660 million in the second quarter of 2018. Purchase money transactions decreased 48% to $196 million in 2019 as compared to $374 million in the second quarter of 2018.

Now I'll touch on some NonQM production results. During the second quarter of 2019, the consumer direct retail channel accounted for 24% of NonQM originations, while wholesale and correspondent channels collectively accounted for 76% of NonQM production. The NonQM originations during the second quarter had a weighted average FICO score of 732 with a weighted average loan-to-value of 70%, which was consistent with prior quarter FICO scores of 728 and an LTV of 69%.

I'll now touch on servicing results. The servicing portfolio generated net income of approximately $4 million in the second quarter ended June 30, 2019, a 64% decrease over the net servicing income of $10 million for the quarter ended June 30, 2018. This was as a result of a $10.5 billion mortgage servicing sale that occurred in 2018. The mortgage servicing portfolio remained flat at $6 billion as of June 30, 2019, as compared to March 31, 2019, but decreased from $17 billion in June of 2018. This is primarily due to the sale of $10.5 billion in the servicing portfolio during the fourth quarter of 2018. This was due to a shift in strategy during the second half of 2018 to direct our

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efforts to reposition the company to focusing on our core noncore -- NonQM lending business and to strengthen our liquidity position.

As a result of the shift in strategy, the MSR assets decreased to $50 million in June of 2019 as compared to $60 million in March of 2019 and down from $181 million in June of 2018.

I'll now touch on our liquidity characteristics. As of June 30, our total warehouse borrowing capacity was $900 million with borrowings of $363 million and available MSR financing of additional $30 million, providing substantial liquidity for the company.

With respect to expenses in the second quarter of 2019, total expenses excluding impairment charges were $22 million as compared to $37 million during the second quarter of 2018. This was a 41% decrease in total expenses. For the 6 months of 2019, total expenses were $44 million, excluding impairment charges as compared to $72 million in total expenses, which included impairment charges during the first 6 months of 2018. This is a 39% decrease in total expenses over the period.

The company will continue to align capacity and expenses with loan origination volume in 2019. To support the increase in originations in Q2 and expected Q3 originations, we've hired 29 employees in the month of June. During Q2 of 2019, personnel expense decreased 14% or $3 million to $14 million from -- down from $17 million in Q2 of 2018. This decrease is primarily related to staff reductions during 2018 and into 2019 as well as reduction in commission expense to decreased loan origination volume.

Headcount decreased 14% to 397 in the second quarter of 2019 as compared to 462 for the same period in 2018. Business promotion decreased by $7 million from Q2 2018, $2 million for the second quarter of 2019, which compares to $9 million for the same period in 2018. Year-over-year decline in business promotional costs confirms our methodology of streamlining and steering towards cost-effective promotion expenses. We moved away from expensive TV media spend and the favorable interest rate environment has driven more organic leads to the platform.

General and administrative expenses decreased 51% to $5 million for the 3 months ended June 30, 2019, which compares to $11 million for the same period in 2018. This concludes financial results for the quarter.

I'd like to turn the call back over to George.

George A. Mangiaracina ***Impac Mortgage Holdings, Inc. - Chairman & CEO***

Thanks, Brian. So in closing, the management team is encouraged by the second quarter results yet. We fully recognize that these are the early innings of the turnaround of the company and that much means to be accomplished. As I noted earlier, the second quarter is the first reporting period with a positive result in either GAAP income or core earnings since new senior leadership team of the company was fully installed in August of 2018. The results evidence the support of the company's capital partners, Board of Directors and the hard work and commitment of our senior leadership team and dedicated employee base. We've stabilized the organization by creating a liquidity margin of safety, secured by our sale of over $10 billion in MSRs in 2018, $7 billion of which was sold when U.S. 10-year treasury rate stood at north of 3%. We remain committed to maintaining a diversified product and channel offering. The GSE-driven call center and the NonQM-driven TPO businesses are complementary. The call center is scalable, providing high-volume at moderate margins in the refi environment, and TPO through NonQM produces interest rate inelastic volume at superior relative margins.

When taken together, our products and channels permit the company to monetize near-term opportunity and concurrently to drive long-term franchise value creation for our capital partners. The company continues to pursue vertical participation in the NonQM asset class for retention of subordinate tranches of private-label securities backed by our NonQM loans. Impac's NonQM credit selection acumen facilitates alignment with strategic capital partners who seek the design portfolios of loans for investment or securitization within permanent capital vehicles. These vehicles would provide the company with access to a stable and efficient source of capital, external to the company's balance sheet, in order to retain interest and the economics of the loans we create. The company's intent would be to participate in the recurring asset management and promote fees from these activities.

I'd like to thank you all for your time and focus this morning. That concludes our prepared remarks. We'll now open the call for questions. Thank you.

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QUESTIONS AND ANSWERS

Operator

Our first question comes from the line of Trevor Cranston from JMP Securities.

Trevor John Cranston ***JMP Securities LLC, Research Division - Director and Senior Research Analyst***

Congratulations on a nice quarter, and it sounds like a nice start to the third quarter as well. Question, I mean, so I appreciate the comments around the size of the refinanceable universe, I think you made in your prepared remarks, George. Just curious, if you could talk about, for example, if rates were just to sort of stabilize where they're at today, so how that translates into the pipeline for you guys? And how long you would expect to see continued high refi volumes coming through in terms of how long you can continue operating capacity? And then when it might start to peter off or if it's just going to stay here?

Justin Moisio ***Impac Mortgage Holdings, Inc. - Chief Administrative Officer***

Trevor, it's Justin. So regarding that, we've increased both staffing levels and our origination efficiency. So as George indicated, our capacity model indicates that within the call center itself, we have the ability to originate and fund up to $600 million per month. And that's at our current staffing levels. So we do have an opportunity to take down an additional floor in the building to build out the call center further as we grow beyond our current capacity. So regarding headcount, as we indicated at the end of the second quarter, we had 397 total employees. As of today, we're up to 446, and our expectation is headcount is going to grow to about 480 in the middle of this month. We've been very successful on recruited -- recruiting highly talented individuals in the area because we had to backfill some of the attrition that we've experienced simply because of the high demand for mortgage professionals in Orange County. So we'll continue to staff thoughtfully and respond appropriately as the market changes, but we think we're in a pretty good spot right now.

Trevor John Cranston ***JMP Securities LLC, Research Division - Director and Senior Research Analyst***

Okay, got it. That's helpful. So I guess, that sort of addresses the question on personnel expense going forward. You guys talked a bit about the shift in strategy with respect to business promotion. I was wondering if you can elaborate a little bit on that? And how we should think about the business promotion expense trending as we go into the third quarter?

Rian Furey ***Impac Mortgage Holdings, Inc. - President of Direct Lending & COO***

Trevor, it's Rian Furey. Business promotion, I think we said was $2 million in Q2. And we've dramatically reduced that spend going into the third quarter. Really, right now, organic demand from consumers is what's driving the volume in the call center, it's not marketing. So we would see, I think, that in the third quarter, as we start to again spend in business promotion, it will be more focused on the NonQM product. Right now, the media is really doing the advertising for us for the conforming refinance business, but we do have an eye on keeping NonQM volumes up, and that does require marketing. So now that we've been able to increase our capacity, you'll see us spending into the NonQM space, but nothing to the magnitude of what we've done in like the first quarter.

Trevor John Cranston ***JMP Securities LLC, Research Division - Director and Senior Research Analyst***

Got you. Okay. And as you guys are seeing higher origination volumes come through, can you talk about how you're thinking about the MSR? And given the lower level of rates, if you think it's an attractive time to be retaining the servicing on originations? Or if you guys are going to continue to look to sell off some of that?

George A. Mangiaracina ***Impac Mortgage Holdings, Inc. - Chairman & CEO***

Well, this is George, Trevor. I'll say that we made a decision last year that the MSR portfolio was outsized given our capital base. And so we had like maybe $16 billion to $18 billion in the beginning of '18, we sold $11 billion of that off last year. We ended this year with just $6 billion in Freddie Mac servicing. And this year, we've been selling all of our GSE servicing product released. So we -- and so we have not been adding to the portfolio. Right now, it's not our intent to add to the portfolio. I think the -- if we continue to drift lower in rate, and we have a multi-year refi wave here, then the servicing is going to run off pretty quickly. And, Brian, maybe you want to jump in a little bit on our views on servicing.

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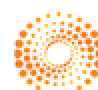

Brian P. Kuelbs ***Impac Mortgage Holdings, Inc. - Executive VP & CFO***

Sure. I think that we've got a much better balance between servicing that we're retaining on balance sheet in our production capabilities, and you really see that through the cash call production in this market environment. And that was part of the reset of the balance sheet last year was to make sure that our market value exposure to rates with respect to the servicing value that we retain is sufficiently sized relative to our production capabilities to replace runoff and ideally generating incremental revenue through the production franchise. And so I think we've seen that in Q2 play out as planned financially, and we'll continue to monitor the MSR position that -- I think our view is not to add to it for the foreseeable future.

George A. Mangiaracina ***Impac Mortgage Holdings, Inc. - Chairman & CEO***

And we are adept at defending the portfolio. We captured about half of -- in the second quarter anyway -- we captured about half of the runoff. First quarter was a little bit less than that, and we have trigger campaign. So we can respond quickly if a consumer is out for a credit down, and we believe they're going to refinance, we try to recapture that loan. But I will say that our capture activity is now fully, and it has been for several years now -- managed by a salaried-only retention team, not a commission LO team. And so we're being mindful of the speeds on our portfolio. We're not attempting to create speed. We're simply defending the portfolio when competitors are approaching customers that are in the MSR book.

Trevor John Cranston ***JMP Securities LLC, Research Division - Director and Senior Research Analyst***

Got you. Okay, that's good to know. And last question, I appreciate the commentary you guys provided around the expiration of the QM patch and the potential size of the addressable market there. I was wondering if you talk about sort of how you guys are thinking about that strategically? And how you expect the market to evolve in the sense of if that sort of NonQM market were to expand fairly dramatically? If you guys are expecting a lot more entrants to come into the market over the next couple of years? And if that's the case, sort of how you guys are planning to maintain a competitive advantage as potentially more people are competing for that type of product?

Nima Vahdat ***Impac Mortgage Holdings, Inc. - General Counsel***

Trevor, this is Nima. So we -- I mean, we do -- we are expecting more entrants into the space. We have seen more entrants in the space as we started in 2014, maybe we're one of the first in the space. So we have well over tens in the space now. And with the expiration of the patch that will definitely increase just by virtue of the fact that so much of their volume will be diverted away from the GSEs that they're currently delivering to. In terms of strategically, I think the fact that we have such a time advantage in terms of delivery outlets and opportunities for sale of those loans puts us well ahead of the game. We also are very experienced in originating this type of mortgage. And we've dedicated the past several years into building out teams specifically focused on this type of lending. And I think that expanding that footprint with the existing head start that we've got puts us in a good space.

Operator

And that concludes our question-and-answer session. I would like to turn it back to our presenters for any further comments.

Justin Moisio ***Impac Mortgage Holdings, Inc. - Chief Administrative Officer***

Thank you for joining us on our second quarter earnings call. We'll be back speaking to the market in early November. Thank you.

Operator

And this concludes today's conference call. Thank you for your participation. Have a wonderful day, and you may now disconnect.

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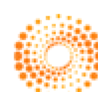

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