FHN FINANCIAL
CAPITAL ASSETS CORP.

JULY 1, 2020
WEEKLY COMMENTS

WORKING TO BE OPPORTUNISTIC IN THIS MARKET

Since the directive was issued by the FHFA in March preventing Fannie Mae and Freddie Mac from buying loans seasoned over six months, many of our customers are finding themselves facing difficulties managing balance sheet challenges that always seem to rise in turbulent markets. Since the early 1980s, seasoned bulk sales have been an efficient way to generate a pool of cash relatively quickly that can be used to address myriad balance sheet management issues such as funding new loans, managing LTD ratios, concentration risk, IRR, etc. While the timeframe for when this suspension may be lifted is unknown, what is known is that these challenges for many are real and must be dealt with now. Today, I will discuss some interim patches that may help relieve some of that pressure.

The typical bank and credit union FHN Financial Capital Assets Corp. (Capital Assets) works with operates a community lending business model with secondary market capability. This is vastly differently from mortgage banking whereby 100% of loans originated are sold. In contrast, most Capital Assets customers hold the majority of their new loans on balance sheet to earn the income, but also sell some loans on a somewhat regular basis to as part of a long-term balance sheet management strategy. In a relatively stable market this system works well, but as every institution knows, unexpected things can and do happen! There are literally dozens of challenges that can pop up and in most cases, the solution requires a strategy that is redeployed in some manner to address the issue at hand. Simply increasing the number of new loans you sell will not generate the required liquidity in the required timeframe.

No 2020 business plan contemplated a pandemic in March and all the resulting issues that followed. In early March 2020, interest rates dropped to historic lows and most Capital Assets customers quickly found themselves dealing with overwhelming volumes of new loans that taxed their operational capacity. When PPP was rolled out as part of the CARES Act, additional stress was added to the loan operations system. From loan officers and production staff to underwriters and servicing personnel, no area was left unscathed. But for many, the one area that was hit hardest was in secondary marketing, especially dealing with agency loan production. We have had conversions with many lenders that weren't able to keep up with new loan volume, and therefore some of the loans that were meant to be sold didn't get committed and ended up going into portfolio.

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All this leads back to the pause in bulk seasoned purchases under the FHFA directive to Fannie and Freddie. Since the seasoning cutoff is now six months or less, there continues to be an ever-narrowing window available to sell and deliver less than six month old closed loans into the agencies to take advantage of this favorable pricing market.

A number of Capital Assets customers have reached out to us for help with the sale of these newer loans, leveraging our existing expertise in pooling, risk assessment, and agency delivery. Although this does not address the larger issue of loans seasoned over six months, it does help clear the pipeline of loans you intended to sell, which may alleviate pressure on balance sheet concentration at least in the short term.

If your staff resources are limited, Capital Assets can work closely with your staff in defining specific pools of eligible loans, create price efficient strategies, utilize our staff to collect the necessary data to deliver, and then facilitate delivery directly in the Fannie/Freddie selling platforms. We then can deliver back what is needed for the custodial certification and servicing information. All of this ideally can be done with a small amount of assistance from your still overtaxed staff.

We can also perform all of these tasks working under your existing Seller/Servicer number to eliminate any additional contracts or extra documents. We would, however, leverage our expertise in moving into more efficient commitment and delivery methods (for example, mandatory vs. best efforts) and pursue more price efficient techniques to maximize trade economics.

While we continue to work closely with the GSEs in hopes the seasoned bulk window will reopen sooner rather than later, we have the resources and expertise to help with a backed-up pipeline. For more information on how Capital Assets can help, contact your FHN Financial representative or Capital Assets directly at 800.456.5460 so we can discuss what options you may have with some of the newer loans in portfolio. Without sounding alarmist, time is of the essence with the existing six-month seasoning cutoff. Each month that goes by removes potential loans to sell. All we need to get started is a loan tape of your mortgage portfolio and we can begin our review and come back with recommendations and solutions.