

TAKING ADVANTAGE OF MARKET OPPORTUNITIES

The onset of COVID-19 and shelter in place has completely disrupted the non-agency Private Label Securitization ("PLS") market. Billions of dollars of new production loans are sitting on the balance sheets of non-bank aggregators, conduits, and securitizations who are anxiously looking for a home for their loans. Loan types include super-prime full doc jumbos, non-QM mortgages, HELOCs, and auto loans, all originated for a PLS takeout that no longer exists. In addition, FHLMC and FNMA have temporarily suspended agency-grade bulk sales. The vast majority of FHN Financial Capital Assets Corp. (Capital Assets) depository customers had no part in causing the PLS market disruption, but most are well positioned to take advantage of it. Loans that were trading at hefty premiums just a few weeks ago are now pricing at discounts to modest premiums. The window of opportunity is open to acquire A grade credit loans at yield spreads very wide to MBS. If resources are an issue, Capital Assets can help by managing many of the typical buyer responsibilities.

Securitization Market Disruption

Because of the collapse of the PLS market, originate-to-sell non-bank originators like mortgage companies and securitization conduits are stuck with loans they can't sell to their typical investors. These highly leveraged non-banks make or buy loans for the express purpose of immediately selling them. In contrast, the majority of middle market/community-size banks and credit unions hold far more loans than they sell, either on a flow or bulk sale basis. For the non-bank companies, the loss of a PLS takeout has been devastating. Many are facing margin calls and desperately need liquidity. The decline in new issue PLS has had a dramatic negative impact on the price of these loans. Using the non-QM market as an example, as little as six weeks ago, originate-to-sell loans were trading at 2%, 3%, and 4% premiums, depending on the characteristics of the loans. Within a very short period, pricing eroded to the high 90s, then to the mid-90s, and in the past week fell to the low 90s. At present, loans classified as non-QM are trading in the mid- to high-80 range. Most Capital Assets customers would not buy non-QM loans, but what's happened in this market has leaked over to super-prime full doc QM loans as well. The price decline is not as bad, but the opportunity is about as good as it gets to buy loans like those you would make for your portfolio at an attractive price.

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Unique Opportunity for Depository Investors

Because of their capital and funding structure, banks and credit unions are uniquely positioned to take advantage of the current situation. Net loan growth is at the top of the list of most every yearly business plan. Most institutions have the ability to fund investments, including a loan purchase, out of readily available cash or with a structured FHLB advance. The economics can be excellent. For example, in a normal market, the typical spread over MBS earned when buying a pool of prime credit mortgages is 100bps+MBS. Today, that spread for the same credit quality is much wider.

So, why isn't everyone lining up to take advantage of this rare opportunity? There are typically two reasons:

- #1 Why should I buy loans when we are making tons of new mortgages? — Most everyone is processing a large volume of new production loans. Unfortunately, a significant number of new loan originations are refinances of existing loans, which doesn't convert to net loan growth. And even if many new refs are other lenders, it's a likely bet that other lenders have refi'd many of your loans as well. But, a purchase of prime credit mortgages of the type and quality you would originate for portfolio "at a better yield than you can originate the same loan type" will definitely help contribute to net growth.
- #2 We are resource constrained processing PPP and a large pipeline — Shelter in place for employees processing large pipelines of new mortgage loans is not an ideal working condition. Strategically speaking, taking advantage of the predicament that non-banks are in makes total sense, but buying a pool of loans can be labor-intensive and time-consuming. We at Capital Assets are acutely aware of how busy everyone is, which is why we are bringing more of our resources to bear than normal. This includes us performing many tasks that the buyer normally does in order to minimize the distractions.

This market opportunity is too attractive to overlook and will likely be short lived. The time to strike is now, and working with Capital Assets can be an incredibly efficient, low-impact way to acquire these high-yield loan assets. In addition to sourcing loans and providing an economic and risk profile assessment of your portfolio, we also manage nearly all of the operational aspects of a loan sale transaction. In short: we do all the heavy lifting. This allows investors to be able to take advantage of the current market opportunities, while still being able to manage the challenges and demands of this unique time.

To learn more about taking advantage of the current market opportunities, please contact me at 866-561-5041.

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