

Don't Just Wait — Prepare

Challenges for depositories have been building for months and new ones are likely on the horizon. If there is one thing this year has taught us it's to expect the unexpected. Added to the list of challenges is the temporary suspension of seasoned bulk sales to Fannie Mae and Freddie Mac that is about to enter its third month! The pause in bulk sales shut the door on one of the most important balance sheet management tools depositories rely on, which is the ability to sell prime-credit, seasoned mortgage loans as part of a structured balance sheet strategy. We at FHN Financial Capital Assets Corp. (Capital Assets) believe we are closer to the end of this suspension than the beginning, and as soon as the massive pipeline of flow loans begins to wane and facts emerge about the lower risk of seasoned portfolio loans, such as the type our customers make, the seasoned bulk path will reopen. Just "waiting" for the window to open could mean you face a mad dash to get in line if you postpone all the prep work until the greenlight turns on. Now is not the time to wait for something to happen. Now is the time to prepare for it.

Capital Assets does business with literally thousands of depository institutions across the country. As we've all struggled with adjusting to life under pandemic conditions, our balance sheets are being impacted in ways that we won't fully understand for months to come. It will be important to be nimble and flexible in the coming weeks and months, which means preparing for the unexpected. One of the most powerful positioning strategies Capital Assets offers is our propriety "Prep-n-Hold" program. A Prep-n-Hold puts you in position to be able to execute the sale of a segment of your older, seasoned loans at the snap of the finger. If you don't need to conduct a sale, no problem, but if a need should arise to generate liquidity to fund new loans, rebalance your portfolio, or a myriad of other strategic initiatives, you can act quickly.

Capital Assets can provide support for multiple balance sheet management challenges starting with a complete analysis of your existing mortgage portfolio to formulate potential solutions to your unique strategic needs. We can also provide the operational and logistical support needed for these types of projects. We know how busy and resource constrained you are, so over the years we have simplified the process into three easy steps:

Step 1: Know your loan portfolio — By far, the most effective way to do this is to submit a loan-level database that our Asset Strategies group will use to conduct a Portfolio Performance Analysis (PPA). The loan PPA is a value-added service offered exclusively to Capital Assets customers that provides an easy and no-cost means to periodically analyze your loans. The PPA will provide you with a detailed breakdown of your loans from a fixed-income point of view, focusing on the composition, interest rate risk profile, liquidity, credit risk — and anything else you could dream about regarding your loan portfolio.

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Asset Strategies will use the PPA as the source document to conduct our newly created Forbearance Risk Assessment (FRA). Forbearance concerns have been a primary issue for the GSEs as the pandemic marched forward. However, for many of our customers, forbearances or deferments have been a small portion of their loan portfolios. By running the assessment, this provides documentation to the GSEs — and regulators — about the limited impact of these loans on your portfolio.

Step 2: Know your options — Our Loan Trading desk then takes the rein — and the PPA results — to model “what if” strategy scenarios. Capital Assets’ Strategy Menu Analysis is a modeling exercise to develop pro forma loan sales, loan purchases, or securitizations designed to achieve different outcomes. Portfolio loans are the primary source of interest income, which is why the vast majority will be held to term, but those assets are there for you to also potentially use some of those loans, if needed, to capitalize on opportunities or resolve challenges that unexpectedly arise. Moreover, because mortgages are so price efficient today, it will be almost impossible to design strategies that do not result in a gain.

You may not need to conduct one or any of the strategies immediately, but the exercise alone will allow you to size up the different strategies to determine which might work best when it is the time to act. Unlike the bond portfolio, this type of flexibility to act with the loan portfolio requires advance planning and preparation — and right now is the time to make those preparations.

Step 3: Be prepared to act — That means taking steps to put yourself in a position where you can actually execute a strategy on a moment’s notice if there is a need. Even highly liquid, investment-grade loans require time to prepare for a potential sale or securitization. In many cases, it makes sense to prepare for a potential transaction that you may never need to execute, but have the ability to execute quickly if the need should arise — we call this a Prep-n- Hold. Because you already have a day job, our Operations department steps in to do the prep work for you by re-underwriting the loans, negotiating an optional securitization commitment, and maintaining the data so you can literally execute a sale of portfolio loans as quickly as selling a bond.

Essentially, a Prep-n-Hold approach is very similar to a full-blown due diligence review associated with a mortgage loan trade strategy. We will develop a list of loans to review (all or a statistically selected sample) and then confirm they adhere to agency guidelines by working from loan images uploaded to our secure site. For instances where we discover differences in documentation and underwriting, we can develop a list of any exceptions or variances that we would normally negotiate with the agencies to allow these loans to trade should a decision be made to do so later.

During this process, we will work closely with your team to prepare detailed reports related to the loans’ liquidity and any other issues we may have encountered during our review. We can also share draft sale agreements to allow your legal team to review and discuss any other issues that may be relevant to this type of project.

The advantages of this approach are numerous, but most significantly this gives you the ability to sell any or all of the loans at a moment’s notice when the GSEs give the greenlight. In addition, the initial sample review will reveal not only any loan underwriting and documentation variances but also any data issues that may exist in your servicing system. Lastly, any file issues related to completeness or accessibility will be revealed so you can address these in the event a more complete review is warranted.

Summary

Capital Assets is a partner that is committed to providing assistance to you in these challenging times. The PPA and Prep-n-Hold is a no-cost service offered exclusively to active Capital Assets customers. The flexibility that this concept allows for is invaluable in today’s more volatile market environment. However, these strategies require your attention. We can help by analyzing the portfolio, determining if a restructuring strategy makes sense for you, re-underwriting the loans, pre-negotiating the commitment, and monitoring the market. When the window opens, we can then lock in a price commitment and facilitate the entire sale and closing process. If you would like more information on the PPA or to setting up a Prep-n-Hold, contact your Capital Assets representative or Capital Assets today at 800.456.5460.

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