

Bob Judge, Government Loan Solutions, Editor



Bob Judge is a partner at Government Loan Solutions.

Government Loan Solutions is a provider of valuation services, pre-payment analytics and operational support for the SBA marketplace.

Bob has 25 years of experience in the fixed income markets. He holds a B.A. in Economics from Vassar College and an M.B.A. in Finance from NYU Stern School of Business.

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## MARCH CPR: PREPAYMENTS FALL BELOW 7%

March prepayments fell below CPR 7% for the 1st time in 2010. In order to put this reading into perspective, it represents the 3rd lowest total since March of 2008.

Specifically, the prepayment speed for March was CPR 6.93%, 14% lower than the February

reading of CPR 8.06%. YTD for 2010 is CPR 7.40%, as compared to CPR 9.71% for the first three months of 2009.

Looking forward to April, preliminary data suggests that prepayment speeds will increase slightly, but remain in the CPR 7% range.

Turning to the default/voluntary prepayment breakdown, the **Voluntary Prepay CPR** (green line) fell below 2% for the first time this decade, recording a VCPR of 1.95%. This reading continues the trend of sub-3% speeds for voluntary prepayments first seen in

*Continued on page 2*

## SMA UPDATE: INCOME POTENTIAL - PREMIUMS, SERVICING, FAS 166

By Jordan Blanchard

Two features in the pending First Lien Mortgage Pool (FLMP) guarantee program 'could' ultimately lead to higher income potential than SBA 7A loans: prepayment penalties and a higher maximum rate.

#### Prepayment Penalty

Long term SBA 7A loans allow only a 5, 3, 1 prepayment penalty for years 1 – 3, but the prepayment penalty flows to the

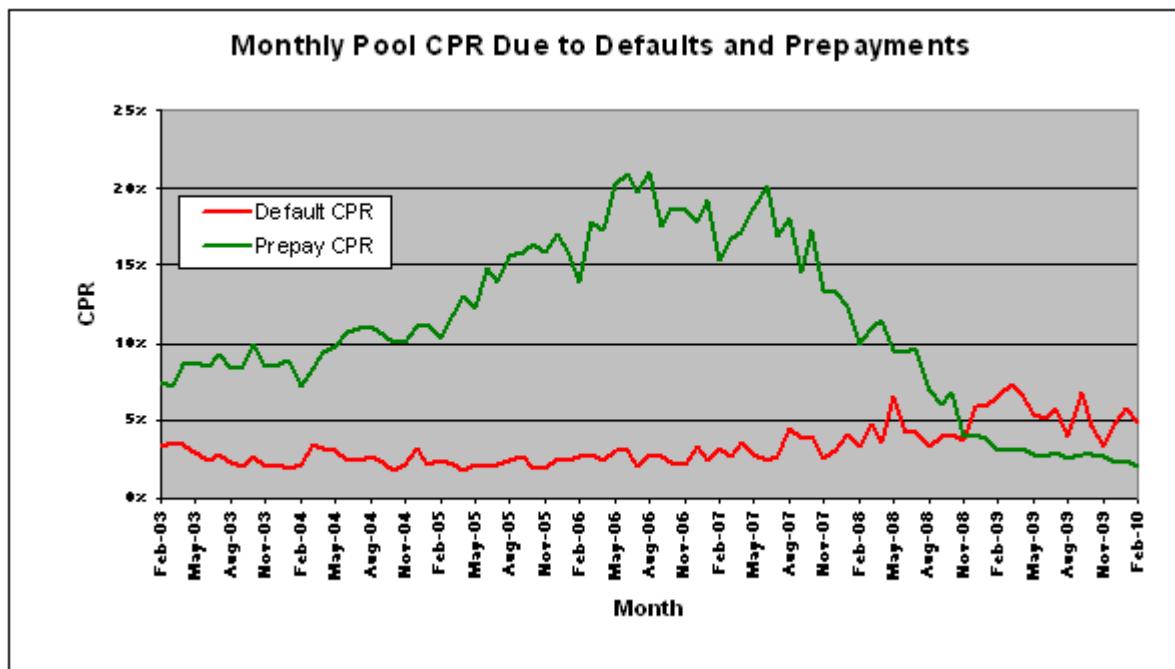
SBA, not the investor. Even so, the introduction of the prepayment penalty by the SBA had a very beneficial effect on premiums because it provided the investor more assurance that the loan would be outstanding for a longer period of time.

10 year prepayment penalty, yield maintenance, or no prepayment penalty at all. The longer and stronger the prepayment penalty, the higher the premium.

*Continued on page 3*



## MARCH CPR...CONTINUED



May of last year. As long as the VCPR remains in this range, overall prepayment speeds should stay below CPR 10%.

While the VCPR hit an all-time low, the **Default CPR** (red line) fell below 5% to DCPR 4.98%, the low end of the 5% to 7% range we have seen since the 1st quarter of 2009. Specifically, the DCPR fell 13% from 5.69% in February.

For March, prepayment speeds fell in three out of the six maturity categories. The largest decrease was seen in the 10-13 maturity bucket, which fell 20% to CPR 8.43%.

Other decreases were seen in the 20+ (-16% to CPR 5.75%) and 13-16 (-6% to CPR 5.37%). Increases were witnessed in the <8 category, which rose by 2% to CPR 10.13%, 16-20 (+1% to CPR 8.69%) and 8-10 (+.48% to CPR 10.05%).

With the first quarter of 2010 in the books, prepayment speeds continue at all-time lows. With very little activity in the voluntary prepayment arena, we expect overall prepayment speeds to continue in the sub-10% area for 2010.

With growing evidence of economic growth in the US economy, we do not expect to see a

spike in default rates outside of the current 5% to 7% range. As long as defaults do not rise significantly, overall prepayment speeds will remain extremely attractive on an historical basis.

From an investors' perspective, this is the time to consider purchasing premium pools and/or IO strips.

*For further information on the terminology and concepts used in this article, please refer to the "Glossary and Definitions" at the end of the report.*

*Data on pages 12-13*

***"With the first quarter of 2010 in the books, prepayment speeds continue at all-time lows. With very little activity in the voluntary prepayment arena, we expect overall prepayment speeds to continue in the sub-10% area for 2010."***

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## SECONDARY MARKET ACCESS...CONTINUED

### Rate

The interest rate cap on SBA 7A loans is Prime + 2.75% (for loans longer than 7 years and greater than \$150,000). The FLMP program has no such restriction, but that does equate to the ability to charge unlimited rates or receive unlimited premiums.

The SBA 504 program itself has a maximum interest rate. Pursuant to 13 CFR 120.921(b), the maximum legal interest rate for any third party lender's commercial loan which funds any portion of the cost of a 504 project (see 13 CFR 120.801) shall be 6% over the New York Prime rate or, if that exceeds the maximum interest rate permitted by the constitution or laws of a given State, the maximum interest rate will be the rate permitted by the constitution or laws of the given State. So currently the maximum interest rate on a 504 first mortgage would be 9.25% for most states. This maximum rate applies to both fixed and adjustable rate loans.

It will be a rare case when the first mortgage lender charges a rate this high, so the rate cap is not nearly as much of an issue as it is with the SBA 7A program. The bigger issue is that whether the first mortgage lender is the pool originator or decides to sell to a pool originator, the premium will reach an upper limit as dictated by the end Investor. The investor has two risks as it relates to premium paid and the corresponding prepayment penalty:

1. The first risk is that the prepayment charged does not cover the premium paid. For instance, if the prepayment penalty is 5, 4, 3, 2, 1, then it is unlikely that the premium will be significantly higher than 5% - although it would not be surprising to see a premium of 8-10%.
2. The second risk is un-collectibility of the prepayment penalty due to SBA regulations. According to CFR 120.921, the third party lender's lien will be subordinate to the CDC/SBA lien regarding any prepayment penalties...in the event of default but only IF the SBA purchases the third party note or purchases the property at the foreclosure sale. It is relatively uncommon for SBA to purchase the first mortgage or purchase the property at foreclosure in the current market environment, but as values increase, the chances of SBA covering increase.

The prepayment penalty does provide significant protection against the risk of borrower refinance, but it does not provide the investor full protection; therefore, there will always be an upper limit on the amount of premium paid by the investor.

### Excess Servicing

So what happens in case where the amount of premium paid by the investor is less than the market value of the loan? For example, assume that a pool originator has a par rate of 6%, pays 1% for

each .25% increase in the rate, but will only pay a maximum of a 4% premium due to a less than desirable prepayment penalty. The pool originator is basically saying that they will pay up to a maximum rate of 7%. What happens if, for example, the note rate is 7.30%? It is expected that the extra 30 bps in this example will become excess servicing.

The SBA has mandated that the seller (the first mortgage lender) retain at least 50 bps in servicing on the sold portion of each loan. So in the prior example, the servicing income to the seller would increase from 50 bps to 80 bps.

### FAS 166

A common question is how much excess servicing will be allowed to qualify the transaction as a true sale. That determination will be made by the accounting firm of the individual bank. For SBA 7A, 100 bps in servicing is the maximum allowed for true sale accounting. But that determination could be a function of the SBA requiring banks to retain at least 100 bps in servicing on a 7A loan. SBA is requiring third party lenders to retain only 50 bps for the FLMP program. Does that mean anything over 50 bps will be considered excess servicing and negate the sale accounting? Only the accountants know. We are waiting for clarification will pass on any findings we receive.

In an effort to prepare for the eventuality of excess servicing (wherever that limit is determined), SMA is actively developing a market for the sale of the residual loan interest for each loan. For example, assume a third party lender sells 85% of a loan to a pool originator, receives premium, and is left with servicing of 120 bps. That level will most likely be considered excess servicing, so the only way that the third party lender will receive sales treatment is to sell the remaining residual portion of the loan. If 100% of a loan is sold along with servicing, then the bank will receive sales treatment. Sale of 85% to the pool originator and 15% to a separate buyer would still be considered a full loan sale.

What about the buyer? Since the buyer is did not make the original loan the buyer is not affected by FAS 166 issues. SMA already has one committed buyer of this residual portion for loans in Southern California. What premiums can be expected? That remains to be seen, but the more buyers, the better the premiums. **If you are interested in becoming a buyer of residual interests in 504 first mortgage loans, please contact Jordan Blanchard at SMA (866-938-4232 or [jblanchard@cdcloans.com](mailto:jblanchard@cdcloans.com)).**

### Due Diligence On Sellers

Are you interested in selling 85% loan interests through Secondary Market Access? If so, SMA needs to perform due diligence on your

*Continued on next page*

## SECONDARY MARKET ACCESS...CONTINUED

organization. Nothing is required from the bank other than an expression of interest since all information can be found via public sources. Please contact Bob Gonzales at 626 354-1560 [bgonzales@cdcloans.com](mailto:bgonzales@cdcloans.com) if you are even considering selling to a pool originator. This will allow SMA to complete this step before prior to program launch.

### Program Status

SBA assures us that they are in the final stages of program creation. SBA expects to provide Colson Services what they need some time during the month of April. The hope is that once this occurs, SBA will be able to announce a formal date for the first pool guarantees (most likely 60 days later). Once a formal date is announced, expect activity to increase significantly.

SMA is also working with SBA and congressional members to consider an extension once the program is launched. Everyone concerned is supportive of an extension.

### Secondary Market Access

Secondary Market Access (SMA) is a consortium of CDC's and financial companies whose main goal is to provide secondary market solutions for 504 first mortgage lenders.

### Our Role

SMA has a solution for every lender need related to the new program, including:

- Sale of the 85% participation interest for premium and servicing income (as described above).

- Sale of the 80% participation interest for those banks who desire to be the Seller and the Pool Originator.
- Sale of the whole loan in situations where the lender is unable to retain any long term portion.
- Sale of the 15% Seller Loan Interest for those lenders that wish to sell 85% of each loan to the Pool Originator and then subsequently sell the remaining 15% to an unaffiliated third party.
- SMA is working on, but has yet to formalize, a solution for excess servicing. Please stay tuned.

SMA is currently looking for eligible funded loans in order to build efficiently-sized loan pools that result in the maximum price paid to the selling lender. If you have loans where the debenture funded on or after February of 2009 (includes first liens funded in 2008), please contact either Jordan Blanchard of CDC Small Business Finance Corp or Bob Judge of Government Loan Solutions. The interested Seller will be sent a loan tape to complete and return. The SMA member will then issue loan bids and coordinate sale for all interested sellers.

### Who we Are

CDC Small Business Finance is the nation's leading SBA 504 Lender and is involved in various other community lending programs. CDC's 504 loan portfolio is comprised of over 3,800 loans totaling \$2B. CDC is a leading innovator in providing solutions to its banking partners and small business borrowers. Jordan Blanchard can be reached at [jblanchard@cdcloans.com](mailto:jblanchard@cdcloans.com), or 951-552-4157.

GLS is a consulting, outsourcing and financial asset valuation company to the small business lending community. GLS is the nationwide leader in the valuation of SBA and USDA loans, servicing rights and securities. For more information about our services, please contact us at (216) 456-2480, or via e-mail at [info@glssolutions.us](mailto:info@glssolutions.us).

## TALF Tracker

The **TALF Tracker**, created by GLS, the same firm that brought you the widely-used "TALF Calculator", is meant to help the TALF investor understand the complexities of their SBA 7a TALF investments.

### Highlights of the TALF Tracker include:

- Track past, present and future payments.
- Create "What-If" scenarios and see their impact on total and net returns.
- See the impact of potential sales prior to the end of the TALF loan period.
- Track investor fees and the net return to investment clients.
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For more information, please contact Rob Herrick, GLS at (216) 456-2480, or via e-mail at [rob.herrick@glssolutions.us](mailto:rob.herrick@glssolutions.us)

## SECONDARY MARKET ACCESS



"The source for accessing the SBA 504 Secondary Market Pooling Program."

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- Pricing bids for existing loans
- Pricing strategies for new loans
- Accepting loan tapes for bid on 85% of eligible loans
- Whole loan sale option
- Assistance with becoming a Pool Originator

If you are 504 lender and wish to discuss how we can help you access the 504 secondary market, please contact:

- Bob Judge, GLS, at (216) 456-2480 ext. 133 or via e-mail at [bob.judge@glssolutions.us](mailto:bob.judge@glssolutions.us)
- Jordan Blanchard, CDC Small Business Finance, at (951) 552-4157 or via e-mail at [jblanchard@cdcloans.com](mailto:jblanchard@cdcloans.com)

## GLS 7(a) Sale & Settlement Tip of the Month

### Sale and Settlement Strategies: Tip #20 – Leave timing to your watch...

We still hear lenders asking when they should sell and to that we almost always respond that timing the market is not a good long-term approach. Never has that been more true than now. Secondary trading levels are exceptionally strong despite being in a post-TALF environment. While we could speculate as to why, the real question is whether or not you are taking advantage of it. As the title says, timing is something best left for your watch, if you have loans to sell, sell them as soon as they are funded and ready to trade.

Scott Evans is a partner at GLS. Mr. Evans has over 18 years of trading experience and has been involved in the SBA secondary markets for the last eight of those years. Mr. Evans has bought, sold, settled, and securitized nearly 20,000 SBA loans and now brings some of that expertise to the **CPR Report** in a recurring article called **Sale and Settlement Tip of the Month**. The article will focus on pragmatic tips aimed at helping lenders develop a more consistent sale and settlement process and ultimately deliver them the best execution possible.



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## GLS VALUE INDICES FALL SLIGHTLY

For February, The GLS Value Indices came in slightly below January, displaying continued stability in the secondary market.

The Base Rate / Libor spread was unchanged at +2.99% and the prepayment element showed minimal declines in speed. These facts, along with stable secondary market prices, equated to minimal changes in the indices.

With FAS 166 beginning in 2010, February was the first month where 25 year, 2.75% gross margin loans breached the 110 level. Without the ability to accept excess servic-

ing, lenders are selling max-margin, long loans above 110 and sharing half the premium above 110 with the SBA. Think of it as SBA lenders contribution to deficit reduction.

Turning to the specifics, five of the six indices moved lower in February while one remained unchanged. The largest decrease was seen in the GLS VI-5, which fell by 20% to 193 basis points. The other decreases were, in order of magnitude, VI-2 (-17% to 155.1), VI-4 (-4% to 192.3), VI-3 (-4% to 150.4) and VI-1 (-2% to 150.8).

The one index that remained unchanged was VI-6, which held steady at 250.7 basis points.

*For further information on the terminology and concepts used in this article, please refer to the "Glossary and Definitions" at the end of the report.*

*Data on pages 9-10, Graph on page 11*

### 7(a) Secondary Market Pricing Grid: February 2010

Maturity	Gross Margin	Fees	Servicing	2/28/2010 Price	Last Month Price	3-Mos. Ago Price	6-Mos. Ago Price	Net Margin
10 yrs.	2.75%	0.6750%	1.00%	108.875	109.00	109.45	109.50	1.075%
15 yrs.	2.75%	0.6750%	1.00%	109.25	109.00	109.53	109.625	1.075%
20 yrs.	2.75%	0.6750%	1.00%	110.00	109.75	110.00 / 1.00%	109.75	1.075%
25 yrs.	2.75%	0.6750%	1.00%	110.125	110.00	110.00 / 1.08%	109.95	1.075%



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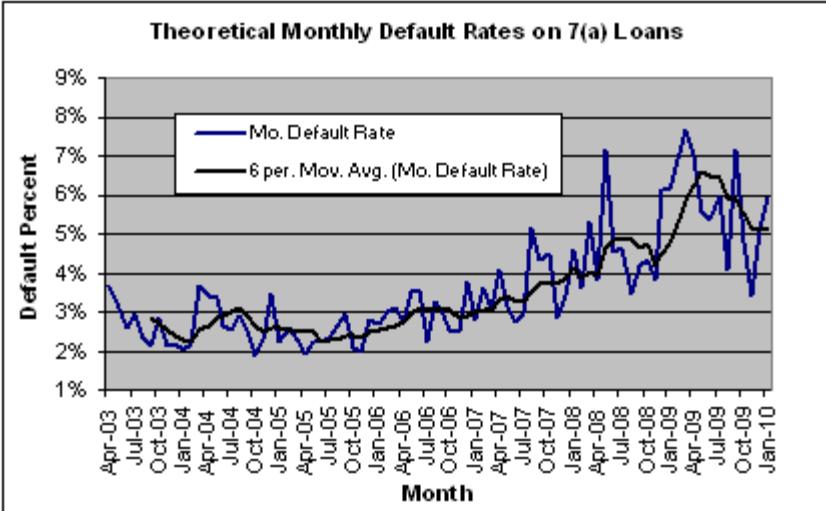
## DEFAULT RATE DECLINES BY 13%

After two months of increases, the theoretical default rate declined by 13% in February, hitting 5.17%.

Since the recession began in December, 2007, the average theoretical default rate on 7a loans has been 5.17%, which by coincidence, is the exact reading for February.

Since we are right in the middle of the recessionary default range, the question now is whether or not we will move toward the high of 7.68% in April of 2009, or back down toward the low of 3.40% in December, 2009.

With evidence suggesting that the economy has begun to grow after 2 years of recession, one would expect the next move to be toward the lows. However, history suggests that the default rate will remain elevated for approximately one year from the end of a recession. For that reason, we believe the range for 2010



will likely be in the 5% to 6% range, with defaults moving closer to the 3% range in 2011.

## DEFAULT-CURTAILMENT RATIOS

In our Default-Curtailment Ratios (DCR) we witnessed a decrease in the 504 ratio for the first time in nine months. Additionally, the 7a ratio exceeded the 504 ratio for the first time since last September.

Please note that an increase in the DCR does not necessarily mean that the default rate is rising, only that the percentage of early curtailments attributable to defaults has increased.

As has been the case for the past 22 months, both ratios continued the trend of recession-level readings of 30%+ for 7(a) and 20%+ for 504 loans.

### SBA 7(a) Default Ratios

For the 22nd month in a row, the 7(a) DCR exceeded 30%, coming in at a record 71.86%, which represents a 2% increase from the previous month's reading of 70.61%.

The 7a DCR remains elevated due to a depressed voluntary prepayment percentage, which hit an all-time low of 1.95% in February. In this case, the denominator

has fallen, thus increasing the percentage of overall prepayments caused by defaults. Turning to actual dollar amounts, defaults fell by \$12 million from January to \$136 million (-8%). As for voluntary prepayments, they also decreased, falling \$8 million (-14%) to an all-time low of \$53 million.

### SBA 504 Default Ratios

Also for the 22nd month in a row, the 504 DCR came in above 20%, falling 6% to 71.80%. While the dollar amount of defaults actually increased, the amount of voluntary prepayments rose by an even greater amount, more than offsetting the increase in defaults.

Specifically, the dollar amount of defaults rose by \$2 million to \$128 million (+2%) in February. As for voluntary prepayments, they increased by \$11 million to \$50 million (+30%).

### Summary

In summary, we are seeing some stability in both DCRs, as defaults are off their near-term highs. Additionally, with voluntary prepayments nearly non-existent, it's hard to imagine the ratios increasing much above the highs seen earlier this year.

*For further information on the terminology and concepts used in this article, please refer to the "Glossary and Definitions" at the end of the report.*

# GLS VALUE INDICES: SUPPORTING DATA

Table 1:

MONTH	BUCKET 1 CPR	BUCKET 2 CPR	BUCKET 3 CPR	BUCKET 4 CPR	BUCKET 5 CPR	BUCKET 6 CPR
Sep-06	20.33%	19.89%	14.29%	18.83%	20.84%	24.55%
Oct-06	19.72%	19.72%	14.32%	19.17%	20.42%	24.51%
Nov-06	18.17%	19.54%	14.82%	19.32%	20.91%	24.83%
Dec-06	16.78%	18.62%	14.44%	18.97%	20.67%	24.48%
Jan-07	16.44%	17.36%	13.95%	18.23%	20.89%	24.14%
Feb-07	17.47%	17.00%	13.86%	17.95%	21.81%	24.21%
Mar-07	16.07%	16.65%	13.54%	17.22%	20.95%	23.23%
Apr-07	16.21%	16.49%	13.55%	17.99%	19.52%	23.13%
May-07	18.09%	17.35%	13.47%	18.38%	19.68%	22.95%
Jun-07	18.39%	17.03%	13.89%	18.96%	20.60%	22.97%
Jul-07	18.52%	17.35%	14.00%	19.55%	20.25%	23.25%
Aug-07	17.72%	17.15%	13.56%	19.48%	18.01%	23.10%
Sep-07	19.18%	17.10%	14.19%	19.85%	18.61%	23.98%
Oct-07	18.14%	17.04%	14.59%	19.16%	18.57%	23.85%
Nov-07	17.68%	16.02%	14.82%	18.87%	18.32%	24.16%
Dec-07	17.14%	15.38%	14.42%	17.22%	17.99%	23.23%
Jan-08	15.70%	14.68%	13.96%	16.44%	17.45%	22.00%
Feb-08	15.91%	13.98%	14.19%	16.20%	17.53%	21.19%
Mar-08	15.58%	13.42%	13.27%	15.08%	15.41%	19.34%
Apr-08	16.16%	13.40%	13.05%	14.59%	15.19%	18.74%
May-08	15.49%	12.93%	12.65%	13.77%	14.33%	17.33%
Jun-08	15.29%	13.36%	12.96%	14.75%	13.62%	17.14%
Jul-08	15.70%	13.03%	12.78%	14.40%	12.49%	16.59%
Aug-08	15.45%	13.28%	12.87%	13.73%	12.24%	15.89%
Sep-08	14.03%	12.49%	12.77%	13.28%	12.36%	15.20%
Oct-08	12.98%	11.67%	12.16%	12.13%	11.97%	14.06%
Nov-08	12.08%	12.36%	11.45%	11.49%	11.49%	13.22%
Dec-08	12.37%	11.81%	10.46%	9.79%	11.08%	11.41%
Jan-09	12.86%	11.55%	10.45%	9.29%	10.61%	10.40%
Feb-09	12.30%	11.30%	10.36%	8.39%	9.99%	9.30%
Mar-09	12.96%	11.97%	10.58%	8.57%	10.47%	8.79%
Apr-09	13.23%	12.34%	11.23%	8.75%	9.81%	8.55%
May-09	13.12%	11.89%	11.80%	8.68%	9.92%	7.98%
Jun-09	13.18%	11.85%	12.36%	8.57%	8.73%	8.02%
Jul-09	12.40%	12.00%	12.51%	8.56%	8.23%	7.36%
Aug-09	13.38%	12.49%	12.36%	8.01%	7.34%	7.21%
Sep-09	12.79%	11.01%	11.83%	7.48%	6.70%	6.89%
Oct-09	12.50%	11.03%	11.35%	7.25%	7.85%	6.79%
Nov-09	12.16%	10.89%	11.05%	6.96%	7.13%	6.32%
Dec-09	11.38%	11.20%	10.59%	7.09%	7.80%	5.75%
Jan-10	11.20%	10.69%	10.34%	6.99%	8.00%	5.75%
Feb-10	10.06%	9.97%	10.05%	7.33%	8.84%	5.71%

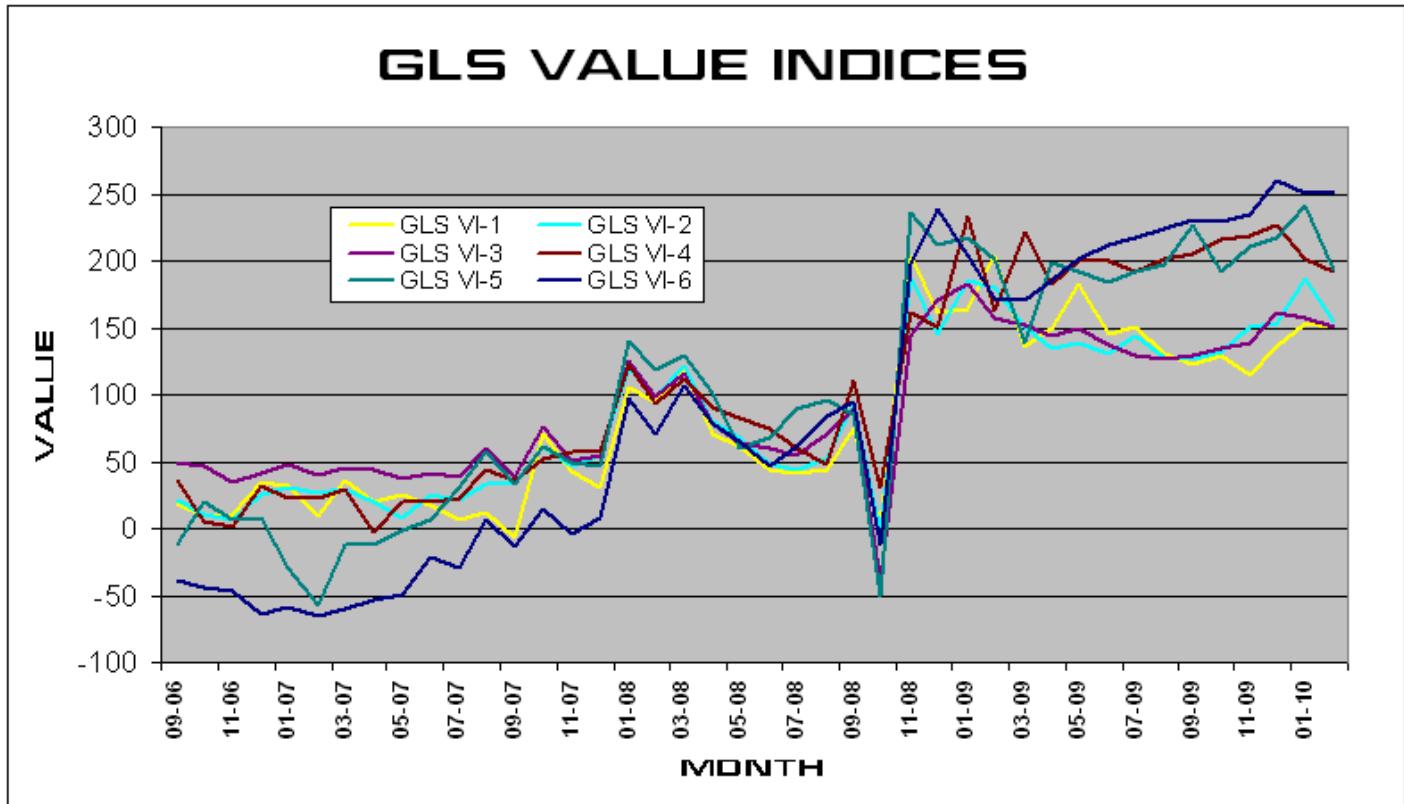
Rolling six-month CPR speeds for all maturity buckets. Source: Colson Services

# GLS VALUE INDICES: HISTORICAL VALUES

Table 2:

MONTH	WAVG LIBOR	WAVG BASE	BASE LIBOR SPD	GLS VI-1	GLS VI-2	GLS VI-3	GLS VI-4	GLS VI-5	GLS VI-6	INDICES LEGEND	
										HIGHEST READING	LOWEST READING
Sep-06	5.37%	8.25%	2.88%	17.8	21.0	49.8	36.2	-12.4	-38.1		
Oct-06	5.37%	8.25%	2.88%	10.0	11.3	46.3	5.4	19.1	-43.5		
Nov-06	5.37%	8.25%	2.88%	10.9	7.0	33.7	1.4	6.2	-46.7		
Dec-06	5.36%	8.25%	2.89%	34.6	24.0	41.1	31.0	8.0	-63.8		
Jan-07	5.35%	8.25%	2.90%	31.0	29.8	48.6	21.3	-30.1	-59.4		
Feb-07	5.36%	8.25%	2.89%	9.2	25.4	39.4	21.3	<b>-57.0</b>	<b>-65.7</b>		
Mar-07	5.34%	8.25%	2.91%	35.9	28.9	45.0	28.5	-12.7	-60.9		
Apr-07	5.35%	8.25%	2.90%	18.8	19.4	43.4	<b>-2.9</b>	-12.5	-53.0		
May-07	5.35%	8.25%	2.90%	24.5	8.5	37.6	18.9	-1.4	-50.0		
Jun-07	5.36%	8.25%	2.89%	16.3	25.2	40.6	18.6	7.0	-22.1		
Jul-07	5.35%	8.25%	2.90%	6.8	20.9	38.1	22.2	30.1	-29.9		
Aug-07	5.48%	8.25%	2.77%	12.9	33.5	59.8	43.6	57.8	7.0		
Sep-07	5.70%	8.21%	2.51%	<b>-7.3</b>	32.2	38.1	36.3	33.3	-14.1		
Oct-07	5.05%	7.74%	2.69%	70.2	61.9	75.6	52.2	61.9	14.6		
Nov-07	4.96%	7.50%	2.54%	42.6	46.7	50.5	57.8	48.7	-4.3		
Dec-07	5.02%	7.35%	2.33%	30.4	55.2	54.4	57.0	46.7	7.9		
Jan-08	3.77%	6.86%	<b>3.09%</b>	105.1	118.6	124.7	121.4	140.1	96.8		
Feb-08	3.10%	6.00%	2.90%	94.4	98.7	98.6	93.3	118.0	69.9		
Mar-08	2.90%	5.95%	3.05%	118.1	120.5	116.2	112.0	128.8	107.4		
Apr-08	2.81%	5.25%	2.44%	69.9	79.5	77.4	90.6	100.8	77.4		
May-08	2.78%	5.15%	2.37%	61.2	66.7	64.1	82.9	60.5	65.1		
Jun-08	2.67%	5.00%	2.33%	44.1	47.4	59.8	74.6	66.9	47.2		
Jul-08	2.75%	5.00%	2.25%	41.7	43.4	55.3	60.8	89.1	61.6		
Aug-08	2.74%	5.02%	2.27%	44.0	52.5	70.1	47.4	95.8	83.1		
Sep-08	3.00%	5.00%	2.00%	73.3	91.2	88.5	111.3	85.2	94.2		
Oct-08	4.43%	4.56%	<b>0.12%</b>	2.3	<b>-3.1</b>	<b>-38.6</b>	30.5	-51.0	-12.9		
Nov-08	2.06%	4.00%	1.94%	<b>203.9</b>	<b>187.0</b>	143.2	161.1	236.0	196.6		
Dec-08	1.64%	3.89%	2.25%	162.2	144.9	170.3	151.0	212.5	238.6		
Jan-09	1.11%	3.25%	2.14%	164.8	185.5	<b>181.7</b>	<b>233.2</b>	218.3	204.4		
Feb-09	1.15%	3.25%	2.10%	203.6	179.5	157.4	162.9	201.5	171.3		
Mar-09	1.06%	3.25%	2.19%	135.3	150.3	151.6	220.4	138.0	169.7		
Apr-09	0.96%	3.28%	2.32%	149.4	134.8	144.3	182.0	198.3	184.5		
May-09	0.70%	3.26%	2.57%	182.1	138.7	149.6	200.3	192.4	200.8		
Jun-09	0.55%	3.25%	2.70%	144.8	130.3	137.3	200.2	183.8	212.8		
Jul-09	0.48%	3.25%	2.77%	150.9	143.8	129.1	191.9	192.4	217.4		
Aug-09	0.39%	3.25%	2.86%	129.7	127.4	125.7	201.7	197.3	222.8		
Sep-09	0.29%	3.25%	2.96%	122.0	126.5	128.3	205.5	225.3	229.6		
Oct-09	0.26%	3.25%	2.99%	128.2	131.3	133.9	216.0	191.2	228.8		
Nov-09	0.26%	3.25%	2.99%	115.3	150.9	138.0	219.2	210.8	234.2		
Dec-09	0.25%	3.25%	3.00%	136.1	153.4	162.0	226.3	218.0	<b>259.6</b>		
Jan-10	0.25%	3.24%	2.99%	153.9	186.5	157.2	201.0	<b>240.6</b>	250.7		
Feb-10	0.25%	3.23%	2.99%	150.8	155.1	150.4	192.3	193.0	250.7		

GLS VI values for all maturity buckets for last 42 months.



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## YTD PREPAYMENT SPEEDS

Table 3:

CPR/MO.	<8	8 - 10	10 - 13	13 - 16	16 - 20	20+	ALL
<b>Jan-10</b>	11.09%	7.10%	9.64%	10.02%	6.92%	5.69%	<b>7.22%</b>
<b>Feb-10</b>	9.89%	10.00%	10.52%	5.73%	8.62%	6.88%	<b>8.06%</b>
<b>Mar-10</b>	10.13%	10.05%	8.43%	5.37%	8.69%	5.75%	<b>6.93%</b>
<b>Grand Total</b>	<b>10.36%</b>	<b>9.07%</b>	<b>9.54%</b>	<b>7.06%</b>	<b>8.08%</b>	<b>6.11%</b>	<b>7.40%</b>

2010 monthly prepayment speeds broken out by maturity sector. Source: Colson Services

Table 4:

POOL AGE	<8	8 - 10	10 - 13	13 - 16	16 - 20	20+	ALL
<b>Jan-10</b>	23 Mos.	27 Mos.	29 Mos.	64 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>
<b>Feb-10</b>	23 Mos.	27 Mos.	30 Mos.	63 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>
<b>Mar-10</b>	23 Mos.	27 Mos.	30 Mos.	63 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>

2010 pool age broken out by maturity sector. Source: Colson Services

## YEAR-TO-DATE CPR DATA

Table 5:

<b>&lt; 8 BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	7.89%	14.51%	11.18%	11.74%	11.13%
<b>Feb-10</b>	11.68%	10.80%	12.71%	3.42%	3.84%
<b>Mar-10</b>	5.02%	13.90%	11.15%	16.45%	4.27%
<b>Grand Total</b>	<b>8.18%</b>	<b>13.09%</b>	<b>11.69%</b>	<b>10.81%</b>	<b>6.45%</b>

<b>10-13 BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	7.65%	13.02%	10.39%	6.83%	7.40%
<b>Feb-10</b>	6.43%	13.46%	15.61%	4.65%	6.75%
<b>Mar-10</b>	4.40%	13.33%	9.29%	8.42%	4.18%
<b>Grand Total</b>	<b>6.13%</b>	<b>13.26%</b>	<b>11.83%</b>	<b>6.66%</b>	<b>6.04%</b>

<b>16-20 BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	0.00%	22.97%	4.97%	4.83%	2.78%
<b>Feb-10</b>	2.63%	10.96%	11.70%	15.55%	5.80%
<b>Mar-10</b>	6.12%	11.16%	12.46%	14.22%	4.07%
<b>Grand Total</b>	<b>2.96%</b>	<b>15.77%</b>	<b>9.88%</b>	<b>11.78%</b>	<b>4.23%</b>

<b>8-10 BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	7.02%	8.82%	4.18%	2.36%	9.14%
<b>Feb-10</b>	8.69%	11.77%	17.07%	9.41%	4.48%
<b>Mar-10</b>	13.38%	12.23%	8.03%	4.54%	5.46%
<b>Grand Total</b>	<b>9.83%</b>	<b>10.84%</b>	<b>10.23%</b>	<b>5.60%</b>	<b>6.40%</b>

<b>13-16 BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	0.00%	8.61%	17.67%	0.00%	10.39%
<b>Feb-10</b>	0.00%	7.81%	0.00%	9.61%	6.50%
<b>Mar-10</b>	3.99%	0.00%	7.18%	8.23%	5.52%
<b>Grand Total</b>	<b>1.60%</b>	<b>6.18%</b>	<b>8.39%</b>	<b>7.56%</b>	<b>7.53%</b>

<b>20+ BY AGE</b>	<b>0-12 Mos.</b>	<b>13-24 Mos.</b>	<b>25-36 Mos.</b>	<b>37-48 Mos.</b>	<b>48+ Mos.</b>
<b>Jan-10</b>	0.35%	6.75%	10.22%	4.75%	6.16%
<b>Feb-10</b>	4.11%	11.32%	10.98%	4.80%	6.19%
<b>Mar-10</b>	1.63%	5.84%	10.60%	6.58%	5.43%
<b>Grand Total</b>	<b>2.09%</b>	<b>7.83%</b>	<b>10.60%</b>	<b>5.37%</b>	<b>5.92%</b>

## GLOSSARY AND DEFINITIONS: PART 1

### Default-Curtailment Ratio

The Default-Curtailment Ratio (DCR), or the percentage of secondary loan curtailments that are attributable to defaults, can be considered a measurement of the health of small business in the U.S. GLS, with default and borrower prepayment data supplied by Colson Services, has calculated DCRs for both SBA 7(a) and 504 loans since January, 2000.

The default ratio is calculated using the following formula:

$$\text{Defaults} / (\text{Defaults} + \text{Prepayments})$$

By definition, when the DCR is increasing, defaults are increasing faster than borrower prepayments, suggesting a difficult business environment for small business, perhaps even recessionary conditions. On the flip side, when the DCR is decreasing, either defaults are falling or borrower prepayments are outpacing defaults, each suggesting improving business conditions for small business.

Our research suggests that a reading of 20% or greater on 7(a) DCRs and 15% or greater on 504 DCRs suggest economic weakness in these small business borrower groups.

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### Theoretical Default Rate

Due to a lack of up-to-date default data, we attempt to estimate the current default rate utilizing two datasets that we track:

1. Total prepayment data on all SBA pools going back to 2003. This is the basis for our monthly prepayment information.

Total prepayment data on all secondary market 7(a) loans going back to 1999, broken down by defaults and voluntary prepayments. This is the basis for our monthly default ratio analysis.

With these two datasets, it is possible to derive a theoretical default rate on SBA 7(a) loans. We say "theoretical" because the reader has to accept the following assumptions as true:

1. The ratio of defaults to total prepayments is approximately the same for SBA 7(a) pools and secondary market 7(a) loans.

**Fact:** 60% to 70% of all secondary market 7(a) loans are inside SBA pools.

2. The default rate for secondary market 7(a) loans closely approximates the default rate for all outstanding 7(a) loans.

**Fact:** 25% to 35% of all outstanding 7(a) loans have been sold into the secondary market.

While the above assumptions seem valid, there exists some unknown margin for error in the resulting analysis. However, that does not invalidate the potential value of the information to the SBA lender community.

### **The Process**

To begin, we calculated total SBA pool prepayments, as a percentage of total secondary loan prepayments, using the following formula:

$$\text{Pool Prepay Percentage} = \text{Pool Prepayments} / \text{Secondary Loan Prepayments}$$

This tells us the percentage of prepayments that are coming from loans that have been pooled. Next, we calculated the theoretical default rate using the following equation:

$$((\text{Secondary Loan Defaults} * \text{Pool Prepay Percentage}) / \text{Pool Opening Balance}) * 12$$

This provides us with the theoretical default rate for SBA 7(a) loans, expressed as an annualized percentage.

---

### GLS Long Value Indices

Utilizing the same maturity buckets as in our CPR analysis, we calculate 6 separate indexes, denoted as GLS VI-1 to VI-6. The numbers equate to our maturity buckets in increasing order, with VI-1 as <8 years, VI-2 as 8-10 years, VI-3 as 10-13 years, VI-4 as 13-16 years, VI-5 as 16-20 years and ending with VI-6 as 20+ years.

The new Indices are basically weighted-average spreads to Libor, using the rolling six-month CPR for pools in the same maturity bucket, at the time of the transaction. While lifetime prepayment speeds would likely be lower for new loans entering the secondary market, utilizing six-month rolling pool speeds allowed us to make relative value judgments across different time periods.

We compare the bond-equivalent yields to the relevant Libor rate at the time of the transaction. We then break the transactions into the six different maturity buckets and calculate the average Libor spread, weighting them by the loan size.

For these indices, the value can be viewed as the average spread to Libor, with a higher number equating to greater value in the trading levels of SBA 7(a) loans.

## GLOSSARY AND DEFINITIONS: PART 2

### Prepayment Calculations

SBA Pool prepayment speeds are calculated using the industry convention of Conditional Prepayment Rate, or CPR. CPR is the annualized percentage of the outstanding balance of a pool that is expected to prepay in a given period. For example, a 10% CPR suggests that 10% of the current balance of a pool will prepay each year.

When reporting prepayment data, we break it into seven different original maturity categories: <8 years, 8-10 years, 10-13 years, 13-16 years, 16-20 years and 20+ years. Within these categories we provide monthly CPR and YTD values.

In order to get a sense as to timing of prepayments during a pool's life, we provide CPR for maturity categories broken down by five different age categories: 0-12 months, 13-24 months, 25-36 months, 37-48 months and 48+ months.

As to the causes of prepayments, we provide a graph which shows prepayment speeds broken down by voluntary borrower prepayment speeds, denoted VCPR and default prepayment speeds, denoted as DCPR. The formula for Total CPR is as follows:

$$\text{Total Pool CPR} = \text{VCPR} + \text{DCPR}$$

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### SBA Libor Base Rate

The SBA Libor Base Rate is set on the first business day of the month utilizing one-month LIBOR, as published in a national financial newspaper or website, plus 3% (300 basis points). The rate will be rounded to two digits with .004 being rounded down and .005 being rounded up.

Please note that the SBA's maximum 7(a) interest rates continue to apply to SBA base rates: Lenders may charge up to 2.25% above the base rate for maturities under seven years and up to 2.75% above the base rate for maturities of seven years or more, with rates 2% higher for loans of \$25,000 or less and 1% higher for loans between \$25,000 and \$50,000. (Allowable interest rates are slightly higher for SBAExpress loans.)

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### Risk Types

The various risk types that impact SBA pools are the following:

**Basis Risk:** The risk of unexpected movements between two indices. The impact of this type of risk was shown in the decrease in the Prime/Libor spread experienced in 2007 and 2008.

**Prepayment Risk:** The risk of principal prepayments due to borrower voluntary curtailments and defaults. Overall prepayments are expressed in CPR, or Conditional Prepayment Rate.

**Interest Rate Risk:** The risk of changes in the value of an interest-bearing asset due to movements in interest rates. For pools with monthly or quarterly adjustments, this risk is low.

**Credit Risk:** Losses experienced due to the default of collateral underlying a security. Since SBA loans and pools are guaranteed by the US government, this risk is very small.

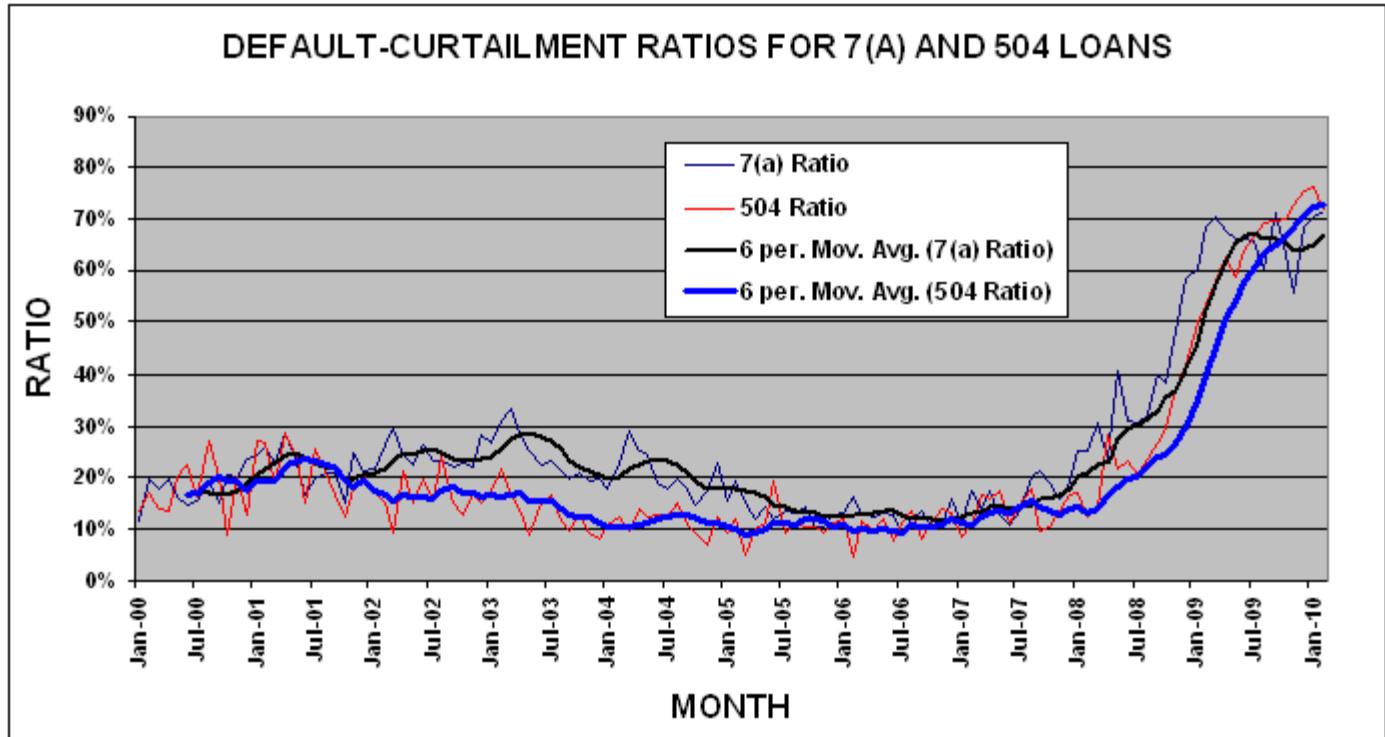
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### TALF

The TALF, or **Term Asset-Backed Security Loan Facility**, was announced by the Federal Reserve Bank and the US Treasury on November 25, 2008. The purpose of the TALF is to make credit available to consumers and small businesses on more favorable terms by facilitating the issuance of asset-backed securities (ABS) and improving the market conditions for ABS more generally.

The Federal Reserve Bank of New York will make up to \$1 trillion of loans under the TALF. TALF loans will have a term of three years; will be non-recourse to the borrower; and will be fully secured by eligible ABS. The US Treasury Department will provide \$100 billion of credit protection to the Federal Reserve in connection with the TALF.

SBA Pools issued in 2008 and beyond are considered eligible securities. SBA Pools are eligible for 3 or 5 year TALF loans. New subscriptions for TALF ended in March, 2010 for SBA-based securities.



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