

Bob Judge, Government Loan Solutions, Editor



Bob Judge is a partner at Government Loan Solutions.

Government Loan Solutions is a provider of valuation services, prepayment 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.

## APRIL CPR: PREPAYMENTS SLIGHTLY ABOVE 7%

Prepayments in April rose slightly from March, moving back above 7% after a one-month respite.

Specifically, the prepayment speed for April was CPR 7.26%, 5% higher than the sub-7% reading in March of CPR 6.93%. YTD for 2010 is CPR

7.37%, which compares favorably to the CPR 9.86% recorded in the first four months of 2009.

Looking forward to May, preliminary data suggests that prepayment speeds will rise above 10%, due to an increase in defaults. Voluntary prepayments should remain below

VCPR 3%, keeping overall prepayments from rising too much into double-digit territory.

Turning to the default/voluntary prepayment breakdown, the **Voluntary Prepay CPR** (green line) rose back above 2%, which is more in-line

*Continued on page 2*

### INSIDE THIS ISSUE:

#### Special points of interest:

- Prepayments Slightly Above 7%
- SMA Update
- Default Rate Declines
- Value Indices Mixed

April CPR	1-2, 14-15
SMA	1, 4-5
The Legal Beat	7
Sale & Settle Tip	8
Value Indices	9, 11-13
Default Rate	10
Default Curtailment Ratios	10 & 18

## SMA UPDATE: PROGRAM START DATE ANNOUNCED

By Jordan Blanchard

### FINALLY!

*Editor's note: Please take the time to check out our new website: [www.SMA504.com](http://www.SMA504.com). It has a wealth of information relating to the new 504 pooling program.*

On Thursday, May 13, SBA announced a date for the first pool application – July 15, 2010. SBA expects the first pools to be settled on or around August 1, 2010. It has

been a long time coming, but the program is finally a reality.

Once again, here are the ways that lenders will be able to benefit from the new 504 pool guarantee program:

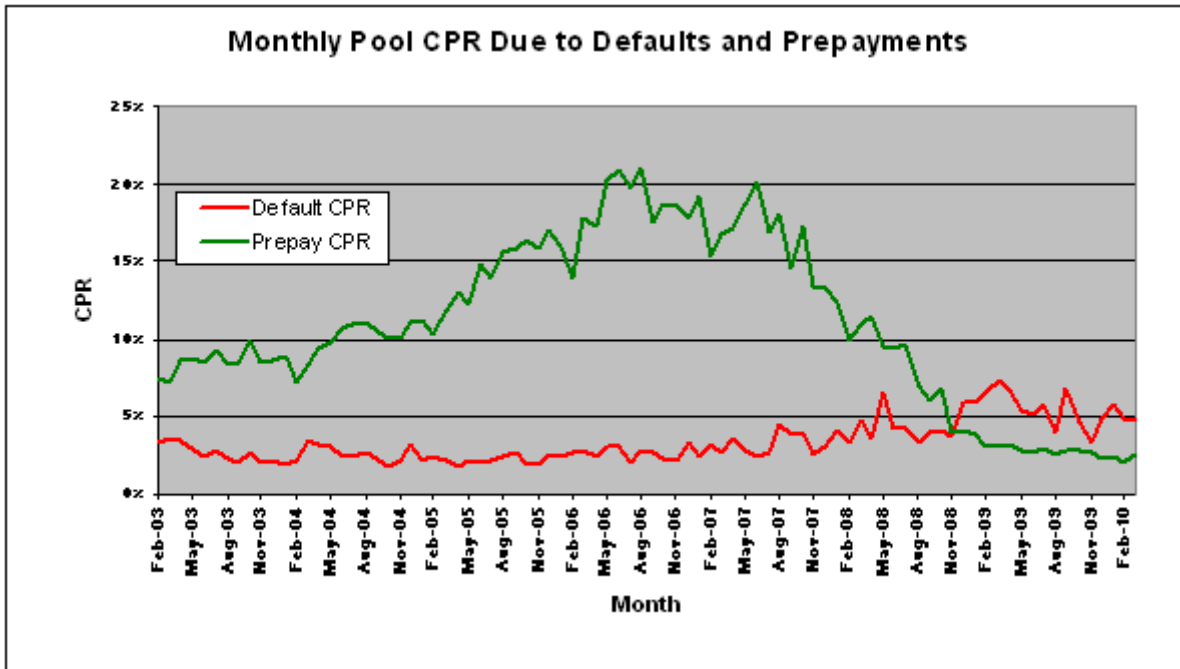
- Sale of 85% participation interests in individual loans. The Third Party Lender will receive premium income on the 85% sold portion of each loan plus a servicing spread of at least 50 basis points (on the entire portion sold).

There is no need for the Third Party Lender to become a Pool Originator under this model. An investment bank Pool Originator will have the ability to form

*Continued on page 4*



# APRIL CPR...CONTINUED



with readings from the past 12 months.

Going forward, voluntary prepayments at, or below, 3% should keep overall prepayment speeds from ranging much above CPR 10%, even in relatively heavy default months.

While the VCPR remained sub-3%, the **Default CPR (red line)** stayed below 5% for the fifth out of the past six months. For the month, the VCPR came in at 4.78%, slightly below the March reading of 4.98%.

For April, prepayment speeds rose in five out of the six maturity categories. The largest increase was seen in the 13-16

maturity bucket, which rose 64% to CPR 8.81%.

Other increases were seen in the 8-10 (+11% to CPR 11.13%), 16-20 (+9% to CPR 9.44%), 10-13 (+7% to CPR 9.06%) and <8 (+2% to CPR 10.37%). Decreases were witnessed in the all-important 20+ maturity category, which fell by 4% to CPR 5.50%, which represents the low for 2010.

While the performance for the first four months of 2010 has been stellar by any measure, the coming increase in defaults next month should concern readers. While we have seen blips in the past and monthly

data can be volatile, it is important to watch for a trend toward higher defaults, which could push overall prepayments above CPR 10% for a prolonged period.

While it is too soon to expect double-digit prepayment speeds to become a trend due to higher defaults, this situation bears watching.

*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 14-15*

***“While the performance for the first four months of 2010 has been stellar by any measure, the coming increase in defaults next month should concern readers.”***

Bob Judge can be reached at (216) 456-2480 ext. 133 or bob.judge@gl solutions.us



## Looking For Warehouse Funding For Your Inventory Of SBA Loans & Pools?



- *For over 25 years, Mark A. Elste, CFA, President of Pennant Management, Inc., has arranged funding for SBA market makers, pool assemblers, and hedge funds.*
- *Let Pennant Management's extensive experience in the settlement of SBA 7(a) and USDA loans help your business today.*



### Contact:

**MARK A. ELSTE, CFA**

414.359.1446 [melste@pennantmanagement.com](mailto:melste@pennantmanagement.com)



CHICAGO      NEW YORK      MILWAUKEE      TAMPA

11270 WEST PARK PLACE, SUITE 1025 • MILWAUKEE, WI 53224 • TEL (414) 359-1044 • FAX (414) 359-1008

[www.pennantmanagement.com](http://www.pennantmanagement.com)

PENNANT MANAGEMENT, INC., IS A SUBSIDIARY OF U.S. FIDUCIARY SERVICES, INC., AN EMPLOYEE-OWNED COMPANY.

## SECONDARY MARKET ACCESS...CONTINUED

large pools (in excess of \$20,000,000 - \$50,000,000 per pool) which will equate to the highest efficiency, and hopefully the highest premium.

Secondary Market Access is the primary agent for at least one major investment bank Pool Originator, to facilitate the sale of 85% participation interests for those banks wishing to pursue this option. Secondary Market Access is accepting loan tapes at this time, and will be issuing rate guidance (rate sheets) on new loans in the next 2 to 3 weeks. Please contact us if you would like to submit a loan tape for an indicative bid.

- The next layer of complexity with 'potentially' higher premium income is for the Third Party Lender to become a Pool Originator, hold 20% on its books, and sell 80% to an investor or broker dealer. It will remain to be seen, however, whether a small loan pool of 2 - 5 first mortgages will sell for more net premium to the Third Party Lender than an efficient \$20,000,000 to \$50,000,000+ pool issued by an investment bank Pool Originator.

Depending on premiums and the volume of the Third Party Lenders wishing to become Pool Originators, it will make sense for some Third Party Lenders to become Pool Originators. Secondary Market Access will be heavily involved in all aspects of this area of the pool guarantee program by providing the following services:

- ⇒ Loan bid solicitation
- ⇒ Loan pricing consultation to attain the best value
- ⇒ Loan funding coordination to achieve the quickest sale
- ⇒ Assistance with procuring CDC/SBA approval of Debenture
- ⇒ Advice on how to minimize Debenture funding timeline (Debenture must fund in order for first mortgage to be pool eligible)

- Quite a number of whole loan buyers are considering entering the secondary market for the purchase of whole loans. In fact, one large lender is expected to announce their involvement in late May or early June.

Secondary Market Access is expected to be one of two primary agents for the purchase and/or direct funding of 504 first mortgages on behalf of this new secondary lender. The good news is that this whole loan buyer (and others considering entering the market) are planning on permanent wholesale loan programs that will exist after the conclusion of the 504 pool guarantee program. It's obvious that the guarantee program is already having the intended effect of jump starting the secondary market for 504 first mortgages.

As a reminder, for the first mortgage to be pool eligible, the SBA

Debenture must have funded on or after February 17 2009 – and as it stands now, before February 2011. Secondary Market Access is working with SBA to possibly redefine the second eligibility requirement in order to extend the effective life of the program. The CDC industry is also working with members of Congress to determine the feasibility of legislatively extending the program to attain the program's original intent: capital for small business expansion and job growth.

The other major requirements for a 504 first mortgage to be pooled are for the payment date to be reset to the 1<sup>st</sup> of every month and electronically debited via ACH. Is this cumbersome? Somewhat, but probably not as much as one would think, and it could very well make the small business borrower very happy. Keep in mind that the SBA debenture is already required to be on ACH, so customer resistance to auto-pay should be minimal. Resetting the payment date will require a Change-In-Terms agreement, but the bank can use this as an opportunity not only to change the date but to modify the terms of the note to be more suitable for sale while still benefiting the borrower. Assume the Third Party Lender holds a first mortgage with an adjustable rate of Prime + 2.00% (currently 5.25%), adjustable quarterly, with little or no prepayment penalty protection. Consider modifying the terms to a 5 year fixed rate at 6.25% with a 5, 4, 3, 2, 1% prepayment penalty. The borrower will be happy because they will be obtaining a long term rate fixed rate in the face of certain rate increases. The Third Party Lender will be satisfied because: A) they kept the borrower from refinancing with another bank, B) made the borrower happy, C) accomplished the required change in payment date and auto deduction, and D) increased their yield over the original terms due to premium and servicing income.

### HR 4302

HR 4302 allows for the maximum debenture to be increased to \$5,000,000. More importantly, HR 4302 also allows for refinancing of owner occupied commercial real estate with the SBA 504 program. If this bill passes it will only mushroom the opportunity and volume of the 504 pool guarantee program. Keep an eye on this pending legislation.

### 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:

*Continued on next page*

## SECONDARY MARKET ACCESS...CONTINUED

- 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@glsolutions.us](mailto:info@glsolutions.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.

For more information, please contact Rob Herrick, GLS at (216) 456-2480, or via e-mail at [rob.herrick@glsolutions.us](mailto:rob.herrick@glsolutions.us)

## SECONDARY MARKET ACCESS



[www.SMA504.com](http://www.SMA504.com)

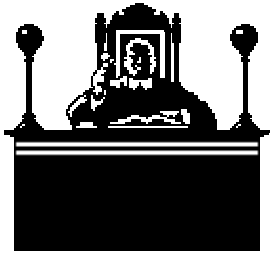
"The source for accessing the SBA 504 Secondary Market Pooling Program."

Providing expertise in all areas of the new SBA 504 First Lien Pool Guaranty program, including:

- 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@gl solutions.us](mailto:bob.judge@gl solutions.us)
- Jordan Blanchard, CDC Small Business Finance, at (951) 552-4157 or via e-mail at [jblanchard@cdc loans.com](mailto:jblanchard@cdc loans.com)



# THE LEGAL BEAT

## BEST PRACTICES: REFINANCING SELLER NOTES

By Ethan W. Smith

In its recent update to the SOP 50 10 5 (B) the SBA imposed new requirements for lenders that seek to refinance seller notes with SBA loans. The requirements, which had previously been included in the section of the SOP pertaining to financing a change of ownership involving intangible assets were overhauled and moved to the section of the current SOP that addresses eligibility requirements for debt refinancing.

Lenders may use SBA loans to refinance seller take-back financing only if:

- The note has been in place for at least 24 months following the change of ownership **and**
- The note is, and has been, current for the past 24 months.

Additionally, lenders should keep in mind that an updated business valuation is required as part of the refinance, if the last valuation was done more than 36 months ago or does not meet the current SBA requirements for business valuations. If the business valuation shows that intangible assets exceed \$500,000.00, the borrower must provide at least 25% in equity injection to process the loan PLP.

These requirements are in addition to the provisions that govern all refinances:

- The loan must have been eligible for SBA financing at the time it was originally made.
- The new installment amount must be at least 10% less than the current installment amount.

Lenders' credit write ups must also contain written analysis answering the following:

- Why was the seller note originally incurred?
- Has over-obligated or imprudent borrowing necessitated major debt restructuring?
- Is the seller note currently on reasonable terms?
- Will the refinance improve the financial condition of the applicant?
- Is the seller note holder in a position to sustain a loss?
- Would the lender/SBA sustain part or all of the same loss through refinancing the debt or will additional collateral or

modified terms protect the taxpayer's interests?

- What portion of the loan is allocated to the refinance?
- If any credit card debt is also refinanced, the borrower must certify that the debt was incurred exclusively for business purposes.

By ensuring that their debt refinancing structure is eligible, especially in the case of refinancing seller take-back notes, Lenders will avoid guaranty denials resulting from ineligible loans. For more information on this and other government guaranteed lending topics, contact the author at [esmith@starfieldsmith.com](mailto:esmith@starfieldsmith.com) or 215.542.7070.

Mr. Smith is a Partner at the law firm of Starfield & Smith, PC.

**Facing a repair or denial  
of your SBA Guaranty?**

**Unsure of what lies ahead?**

**WE CAN HELP.**

**STARFIELD & SMITH, PC**  
ATTORNEYS AT LAW

**Loan Documentation • Closing  
SBA Guaranty Repurchase • Regulatory Compliance  
Franchise Eligibility • Business Consulting**

501 Office Center Drive - Suite 350 • Fort Washington, PA 19034  
(215) 542-7070 • Fax (215) 542-0723 • [www.starfieldsmith.com](http://www.starfieldsmith.com)

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

### Settlement & Sales Strategies Tip #21 – Lengthen IO period? You should.

Consider writing loans with slightly longer interest only periods. Plain and simple, this benefits everyone. For your borrower, it allows them to make lower initial payments. Investors like buying loans while they are still making interest only payments as they receive interest on larger balances. Lastly, lenders can maximize their recognized gain on sale since their loans will not be amortizing over the 90 day warranty period. That being the case, the gain at the end of the contingent liability period will be essentially the same as it was on the day the loan was sold.

*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.*



Increase your premium dollars by eliminating brokerage fees and selling your SBA and USDA Loans “Investor Direct” to Thomas USAF, America’s largest direct investor.

Contact Mike or Vasu at 404-365-2040



## GLS VALUE INDICES MIXED

For March, The GLS Value Indices came in with mixed results, with an equal number of indices rising as falling from February.

The Base Rate / Libor spread was unchanged for the third month in a row at +2.99% and the prepayment element showed minimal movement in speeds.

As loan pricing continues to creep above 110 on max-gross margin loans, the Base Rate / Libor spread near all-time highs and the prepayment element at all-time lows, we expect the indices to begin to fall on a go forward basis. Having said that,

current levels are very attractive on an historical basis and it would take dramatic increases in loan pricing to reach negative index levels last seen in 2007.

Turning to the specifics, three of the six indices moved higher in March while the same number decreased. The largest increase was seen in the GLS VI-5, which rose by 9% to 209.5 basis points. The other increases were, in order of magnitude, VI-4 (+7% to 206.4) and VI-3 (+4% to 155.8).

As for the decreases, the largest was VI-2, which fell by 19% to 126 basis points.

Other decreases were seen in VI-1 (-12% to 133.1) and VI-6 (-.55% to 249.3).

As of the end of March, returns for all maturity buckets, on a Libor basis, still remained attractive.

*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 11-12, Graph on page 13*

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

Maturity	Gross Margin	Fees	Servicing	3/31/2010 Price	Last Month Price	3-Mos. Ago Price	6-Mos. Ago Price	Net Margin
10 yrs.	2.75%	0.6750%	1.00%	109.25	108.875	109.00	109.65	1.075%
15 yrs.	2.75%	0.6750%	1.00%	109.40	109.25	109.125	109.80	1.075%
20 yrs.	2.75%	0.6750%	1.00%	110.05	110.00	109.375	110.00	1.075%
25 yrs.	2.75%	0.6750%	1.00%	110.25	110.125	109.75	110.00	1.075%



**Signature Securities Group, located in Houston, TX, provides the following services to meet your needs:**

- SBA Loans and Pools
- Assistance meeting CRA guidelines
- USDA B&I and FSA Loans
- Fixed Income Securities

For more information, please call  
Toll-free 1-866-750-7150

Securities and Insurance products are:  
• NOT FDIC INSURED • NO BANK GUARANTEE • MAY LOSE VALUE Signature Securities Group Corporation (SSG), member of FINRA/SIPC, is a registered broker dealer, registered investment advisor and licensed insurance agency. SSG is a wholly owned subsidiary of Signature Bank.

## Delinquency Site Inspections?



CSI's 650 field inspectors are wherever you need them, whenever you need them. We specialize in pre-funding, annual due diligence, and delinquent account site inspections.

**Collateral Specialists Inc.**  
A Nationwide Leader in Inspection Services  
**800-252-1057**  
[www.csina.com](http://www.csina.com)

Prefunding Inspections ♦ Delinquency Inspections  
Annual Due Diligence Inspections

## DEFAULT RATE FALLS BELOW 5%

For the first time this year, the theoretical default rate fell below 5%, reaching 4.97% in March.

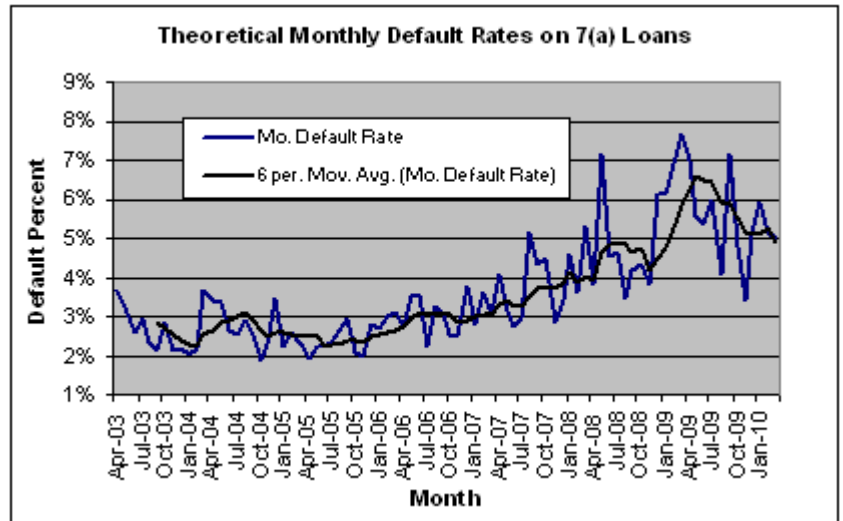
However, this pleasant news should be short-lived, as we expect the default rate to rise above 6% next month to a 2010 high.

While monthly data can be volatile and a few month's results can lead to false conclusions regarding the trend, it is important to remain vigilant. With next month's report, we will see the impact of higher recorded defaults and their impact on the default rate.

Returning to this month's data, the YTD default rate is below the average for 2009.

Last year, the average default rate was 5.78%, while for the first three months of 2010 it is 5.37%.

With the economy growing again, hopefully we are in store for a level, or de-



creasing, default rate in 2010 and 2011. Let's hope next month's results are an anomaly.

## DEFAULT-CURTAILMENT RATIOS

In our Default-Curtailment Ratios (DCR) we witnessed a decrease in the 7a DCR and an all-time high in the 504 ratio. With voluntary prepayments depressed for both 7a and 504 loans, it is no surprise that both ratios are increasing.

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 23 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 23rd month in a row, the 7(a) DCR exceeded 30%, coming in at 65.78%, which represents an 4% decrease from the previous month's reading of 71.86%.

The 7a DCR remains elevated due to a depressed voluntary prepayment percentage, which remained below 2.5% for the fourth month in a row. Once again, the

denominator remained depressed, thus increasing the percentage of overall prepayments caused by defaults.

Turning to actual dollar amounts, defaults rose by \$3 million from February to \$138 million (+2%). As for voluntary prepayments, they also increased, rising \$19 million (+36%) to \$72 million.

### SBA 504 Default Ratios

Also for the 23rd month in a row, the 504 DCR came in above 20%, rising 8% to 77.57%, a new record. With voluntary prepayments near an all-time low, the "low denominator" phenomena is also at work with the 504 DCR.

Specifically, the dollar amount of defaults rose by \$22 million to \$150 million (+17%) in March. As for voluntary prepayments, they decreased by \$7 million to \$43 million (-14%).

### Summary

In summary, we are witnessing a continued

decrease in voluntary prepayments, while defaults remain near the highs for 2009-2010. As long as the main reason for prepayments are loan defaults, the DCR for both 7a and 504 loans will remain elevated.

*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.*

*Graph on page 18*

[www.sma504.com](http://www.sma504.com)  
 "The Informational Source  
 for 504 Pooling"

## 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
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%
Mar-10	9.92%	10.73%	10.11%	7.12%	8.75%	5.75%

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

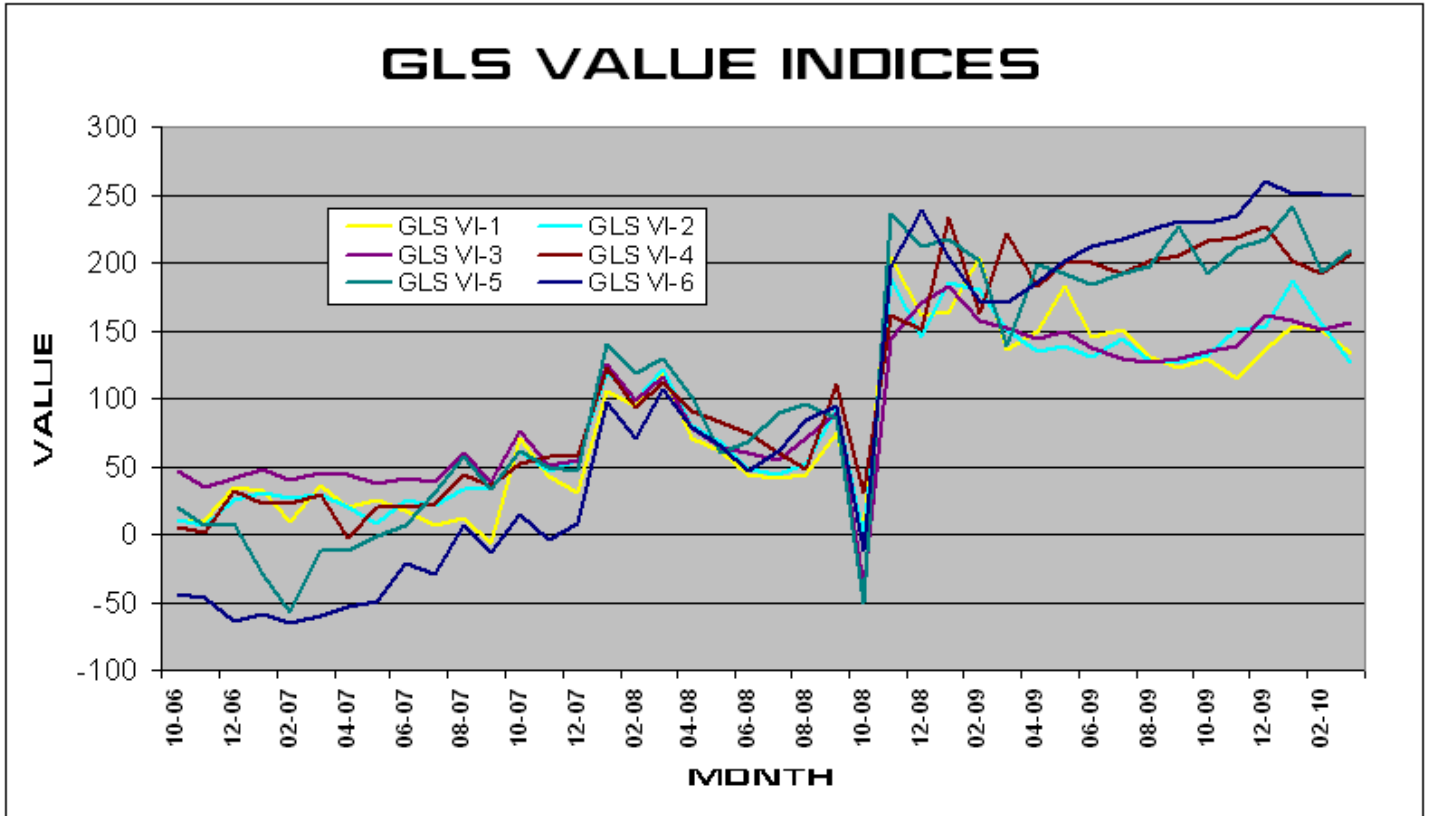
# GLS VALUE INDICES: HISTORICAL VALUES

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
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	-57.0	-65.7
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	-2.9	-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%	-7.3	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%	3.09%	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%	0.12%	2.3	-3.1	-38.6	30.5	-51.0	-12.9
Nov-08	2.06%	4.00%	1.94%	203.9	187.0	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	181.7	233.2	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	259.6
Jan-10	0.25%	3.24%	2.99%	153.9	186.5	157.2	201.0	240.6	250.7
Feb-10	0.25%	3.23%	2.99%	150.8	155.1	150.4	192.3	193.0	250.7
Mar-10	0.26%	3.25%	2.99%	133.1	126.0	155.8	206.4	209.5	249.3

INDICES LEGEND	
	HIGHEST READING
	LOWEST READING

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



## Let GLS Value your Mortgage Servicing Rights

Government Loan Solutions, the national leader in SBA servicing portfolio valuation, now offers its market-based valuation methodology to the mortgage servicing industry.

If your firm provides mortgage servicing, we can provide you with the same loan-by-loan detail and stress testing that we provide to our SBA servicing clients.

For more information, please contact Rob Herrick at 216-456-2480 ext. 144 or by e-mail at [rob.herrick@gl solutions.us](mailto:rob.herrick@gl solutions.us)

## YTD PREPAYMENT SPEEDS

Table 3:

CPR/MO.	<8	8 - 10	10 - 13	13 - 16	16 - 20	20+	ALL
Jan-10	11.09%	7.10%	9.64%	10.02%	6.92%	5.69%	<b>7.22%</b>
Feb-10	9.89%	10.00%	10.52%	5.73%	8.62%	6.88%	<b>8.06%</b>
Mar-10	10.13%	10.05%	8.43%	5.37%	8.69%	5.75%	<b>6.93%</b>
Apr-10	10.37%	11.13%	9.06%	8.81%	9.44%	5.50%	<b>7.26%</b>
Grand Total	<b>10.36%</b>	<b>9.59%</b>	<b>9.42%</b>	<b>7.50%</b>	<b>8.42%</b>	<b>5.95%</b>	<b>7.37%</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
Jan-10	23 Mos.	27 Mos.	29 Mos.	64 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>
Feb-10	23 Mos.	27 Mos.	30 Mos.	63 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>
Mar-10	23 Mos.	27 Mos.	30 Mos.	63 Mos.	46 Mos.	49 Mos.	<b>43 Mos.</b>
Apr-10	22 Mos.	27 Mos.	30 Mos.	63 Mos.	47 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:

< 8 BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	7.89%	14.51%	11.18%	11.74%	11.13%
Feb-10	11.68%	10.80%	12.71%	3.42%	3.84%
Mar-10	5.02%	13.90%	11.15%	16.45%	4.27%
Apr-10	6.20%	14.99%	10.87%	10.88%	13.92%
<b>Grand Total</b>	<b>7.62%</b>	<b>13.58%</b>	<b>11.50%</b>	<b>10.83%</b>	<b>8.41%</b>

10-13 BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	7.65%	13.02%	10.39%	6.83%	7.40%
Feb-10	6.43%	13.46%	15.61%	4.65%	6.75%
Mar-10	4.40%	13.33%	9.29%	8.42%	4.18%
Apr-10	4.32%	13.93%	10.20%	6.87%	9.22%
<b>Grand Total</b>	<b>5.66%</b>	<b>13.41%</b>	<b>11.43%</b>	<b>6.71%</b>	<b>6.91%</b>

16-20 BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	0.00%	22.97%	4.97%	4.83%	2.78%
Feb-10	2.63%	10.96%	11.70%	15.55%	5.80%
Mar-10	6.12%	11.16%	12.46%	14.22%	4.07%
Apr-10	3.64%	0.00%	17.22%	12.88%	8.66%
<b>Grand Total</b>	<b>3.13%</b>	<b>12.45%</b>	<b>11.73%</b>	<b>12.08%</b>	<b>5.37%</b>

8-10 BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	7.02%	8.82%	4.18%	2.36%	9.14%
Feb-10	8.69%	11.77%	17.07%	9.41%	4.48%
Mar-10	13.38%	12.23%	8.03%	4.54%	5.46%
Apr-10	7.54%	19.56%	7.19%	8.07%	10.84%
<b>Grand Total</b>	<b>9.28%</b>	<b>13.13%</b>	<b>9.42%</b>	<b>6.22%</b>	<b>7.52%</b>

13-16 BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	0.00%	8.61%	17.67%	0.00%	10.39%
Feb-10	0.00%	7.81%	0.00%	9.61%	6.50%
Mar-10	3.99%	0.00%	7.18%	8.23%	5.52%
Apr-10	9.54%	34.85%	20.78%	0.00%	7.32%
<b>Grand Total</b>	<b>4.00%</b>	<b>12.87%</b>	<b>11.27%</b>	<b>4.52%</b>	<b>7.48%</b>

20+ BY AGE	0-12 Mos.	13-24 Mos.	25-36 Mos.	37-48 Mos.	48+ Mos.
Jan-10	0.35%	6.75%	10.22%	4.75%	6.16%
Feb-10	4.11%	11.32%	10.98%	4.80%	6.19%
Mar-10	1.63%	5.84%	10.60%	6.58%	5.43%
Apr-10	5.04%	6.76%	7.02%	5.07%	4.93%
<b>Grand Total</b>	<b>2.86%</b>	<b>7.53%</b>	<b>9.76%</b>	<b>5.30%</b>	<b>5.67%</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.

---

### 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:

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

---

### 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.)

---

### 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.

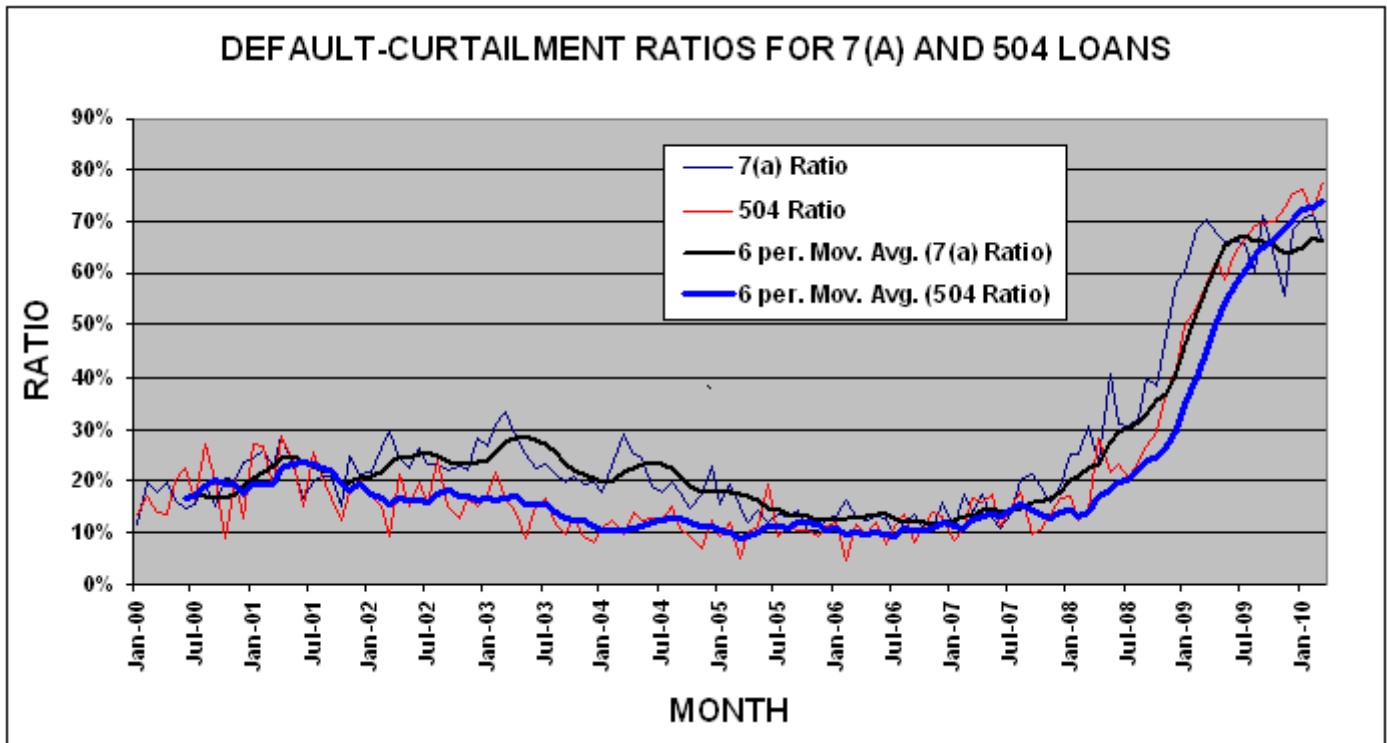
---

### Secondary Market First Lien Position 504 Loan Pool Guarantee Program

As part of the American Recovery and Reinvestment Act (AKA the Stimulus Bill), Congress authorized the SBA to create a temporary program that provides a guarantee on an eligible pool of SBA 504 first liens. The program was authorized for a period of two years from the date of bill passage – February, 2009. The eligibility of each loan is dependent on the date of the SBA Debenture funding. To be eligible, the Debenture must have been funded on or after February 17, 2009, and prior to February 16, 2011. The total guarantee allocation is \$3 Billion.

**The SBA announced that they will begin issuing the first pool guarantees in July, 2010 for early August settlement.**

For the purposes of the program, a pool is defined as 2 or more loans. A pool must be either fixed (for life) or adjustable (any period adjustment including 5 or 10 years). If the pool is comprised of adjustable rate loans, all loans must have the same base rate (e.g. Prime, LIBOR, LIBOR Swaps, FHLB, etc.). Finally, each loan must be current for the lesser of 6 months or from the time of loan funding. Congress mandated that this be a **zero subsidy program to the SBA** (and the US taxpayer). The SBA has determined the program cost (management and expected losses) can be covered by an ongoing subsidy fee of .167%.



## GOVERNMENT LOAN SOLUTIONS

The nationwide leader in the valuation of SBA and USDA assets.

GLS provides valuations for:

- SBA 7(a), 504 1st mortgage and USDA servicing rights
- SBA 7(a) and 504 1st mortgage pools
- Guaranteed and non-guaranteed 7(a) loan portions Interest-only portions of SBA and USDA loans

In these times of market uncertainty, let GLS help you in determining the value of your SBA and USDA related-assets.

For further information, please contact Rob Herrick at (216) 456-2480 ext. 144 or at [rob.herrick@glsolutions.us](mailto:rob.herrick@glsolutions.us)

**POWERED BY:**

Phone: (216) 456-2480  
 Fax: (216) 456-2481  
 Web Site: [www.glsolutions.us](http://www.glsolutions.us)  
 E-mail: [info@glsoptions.us](mailto:info@glsoptions.us)

**Government Loan Solutions**

812 Huron Road  
 Cleveland, OH 44115

**Partners**

**Scott Evans**  
**Bob Judge**  
**Rob Herrick**

[www.glsolutions.us](http://www.glsolutions.us)

Government Loan Solutions' CPR Report is a monthly electronic newsletter published by Coleman Publishing.

The opinions, unless otherwise stated, are exclusively those of the editorial staff.

This newsletter is not to be reproduced or distributed in any form or fashion, without the express written consent of Coleman or Government Loan Solutions.

Government Loan Solutions' CPR Report is distributed in pdf format via e-mail. Spreadsheets relating to the presented data are available to paid subscribers upon request.

The subscription to the Government Loan Solutions' "CPR Report" is free to all members of the SBA Community.

To subscribe, please contact Coleman at (800) 617-1380 or via email at: [bob@colemanpublishing.com](mailto:bob@colemanpublishing.com)

*Government Loan Solutions, Inc. (GLS) was founded by three former Bond Traders in Cleveland, OH. Scott Evans, Rob Herrick and Bob Judge possess a combined 70 years experience in the institutional fixed income markets, 40 of which are in the SBA securitization business. GLS formally began operations in January, 2007. Our mission is as follows:*

*"The purpose of Government Loan Solutions is to bring greater efficiency, productivity and transparency to the financial markets. Through the use of proprietary technology, we intend to aid lenders in all aspects of their government lending, help pool assemblers be more productive in their operational procedures and provide quality research to the investor community."*

**Services available include:****Lenders:**

- *Manage loan sales to the secondary market*
- *Process loan settlements via our electronic platform, E-Settle*
- *Third-Party servicing and non-guaranteed asset valuation*
- *Model Validation*
- *Specialized research projects*
- *Mortgage Servicing Valuation*

**Pool Assemblers:**

- *Manage loan settlements and pool formation*
- *Loan and IO accounting*
- *Loan, Pool and IO Mark-To-Market*
- *Specialized research projects*

**Institutional Investors:**

- *Loan, Pool, and IO Mark-To-Market*
- *Specialized research projects*
- *Portfolio consulting, including TALF*

*For additional information regarding our products and capabilities, please contact us at:*

*Phone: (216)456-2480 E-mail at: [info@glsoptions.us](mailto:info@glsoptions.us) web: [www.glsolutions.us](http://www.glsolutions.us)*

**EDITORIAL DISCLAIMER**

DISCLAIMER OF WARRANTIES – GOVERNMENT LOAN SOLUTIONS (GLS) MAKES NO REPRESENTATIONS OR WARRANTIES REGARDING THE ACCURACY, RELIABILITY OR COMPLETENESS OF THE CONTENT OF THIS REPORT. TO THE EXTENT PERMISSIBLE BY LAW, GLS DISCLAIMS ALL WARRANTIES, EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE.

Limitation of Liability - GLS shall not be liable for damages of any kind, including without limitation special or consequential damages, arising out of your use of, or reliance upon, this publication or the content hereof.

This Report may contain advice, opinions, and statements of various information providers and content providers. GLS does not represent or endorse the accuracy or reliability of any advice, opinion, statement or other information provided by any information provider or content provider, or any user of this Report or other person or entity. Reliance upon any such opinion, advice, statement, or other information shall also be at your own risk.

Prior to the execution of a purchase or sale or any security or investment, you are advised to consult with investment professionals, as appropriate, to verify pricing and other information. Neither GLS, its information providers or content providers shall have any liability for investment decisions based upon, or the results obtained from, the information provided. Neither GLS, its information providers or content providers guarantee or warrant the timeliness, sequence, accuracy, or completeness of any such information. Nothing contained in this Report is intended to be, nor shall it be construed as, investment advice.