Loan PARTICIPATIONS by alloya

LP QUARTERLY

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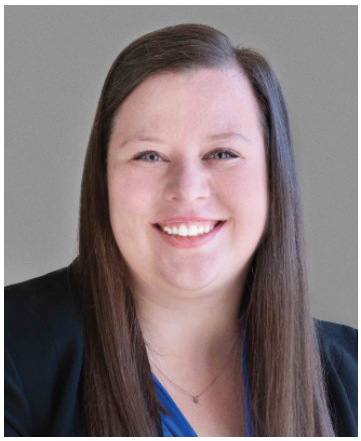
Alloya's Quarterly
Loan Participation Newsletter

IN THIS ISSUE

VOL 3

ALLOYA'S STRATEGIC GOALS

At Alloya, every decision is grounded in our mission to support credit union success and our dedication to three strategic goals: **People, Member Service, and Financial Performance and Compliance.** Alloya's quarterly loan participation newsletter is no exception. We hope you enjoy the latest edition of our quarterly newsletter and subscribe at **www.alloyacorp.org/subscriptions** to receive future issues to your inbox!



GET TO KNOW JESSICA JOHNSON

Alloya's Loan Participation Analyst

We are thrilled to introduce you to the newest member of Alloya's Loan Participation team, Jess Johnson! Based in greater Philadelphia, Jess has a deep understanding of financial markets through her experience in commercial mortgage-backed securities (CMBS) bond analysis. She holds a bachelor's in finance and a Master of Business Administration. In her three months of service at Alloya, Jess has been instrumental in helping develop a new education program that will expand credit unions' knowledge of loan participations while minimizing a common barrier to entry. The program will be launching soon, but until then, Jess is excited to support credit union success through Alloya's Loan Participation Program.

People | Member Service | Financial Performance & Compliance

A COMPARISON OF FINANCIAL RATIOS: BUYERS VS. NON-BUYERS

Achieving Strategic Goals Through Cooperation

You know it, we know it, everyone knows it. Credit unions have seen rapid growth in their deposit levels since Q1 of 2021. Many of us were hopeful at first that funds would flow back out as swiftly as they came in. A year later, it appears that deposited funds will remain parked for the foreseeable future – which means loan demand at many credit unions is likely to stay stagnant.

FORTUNATELY, THERE'S A SIMPLE SOLUTION.

While one credit union might struggle with slow-moving loan demand, another credit union is experiencing a steady influx. The former has excess cash; the latter is bumping up against its concentration limits. The former needs to invest; the latter needs to issue. Call it what you want. Win-win. Symbiosis. You-scratch-my-back-I'll-scratch-yours. You get the idea. What one credit union needs, the other can provide. The proof is in the pudding.

While there are always other variables at play, the takeaway is clear: If you're not investing in loan participations, you ought to be considering it.

	LP BUYERS	LP NON-BUYERS
ASSETS	$890M	$245M
LOAN/SHARE	64%	53%
NET WORTH RATIO	10%	13%
DELIQUENCY RATIO	0.5%	1.18%

"The NCUA continues to encourage credit unions to utilize safe-and-sound practices as they manage their loan participation portfolios, which are often serviced by an outside entity. NCUA examiners will verify that credit unions have evaluated the risk in the loan participation transactions and how that risk fits within the tolerance levels established by the credit union's board. At a transactional level, each loan participation must have separate and distinct records for individual payments, including principal, interest, fees, escrows and other information relating to individual loans. While remittances to the credit union may come in a single payment, credit unions must reconcile this information to the servicer's records and follow prudent third-party due diligence practices when purchasing loan participations."

- NCUA LP Guidance

NCUA RELEASES LP GUIDANCE

The NCUA recently released guidance related to loan participations, specifically pertaining to the compliance of credit union programs.

The due diligence phase is of utmost importance to the health of any loan participation transaction and utilizing Alloya's Loan Participation Platform effectively eliminates the administrative burden associated with due diligence.

For selling credit unions, due diligence is a one-time streamlined process in the Loan Participation Platform. Documentation is uploaded to the platform once and buying credit unions can then access the information as needed. There is no need for sellers to distribute and re-distribute the same documentation each time a new buyer initiates a transaction.

For our purchasing credit unions, due diligence documentation is easily accessible through the platform so they can review it at their convenience as often as they need.

Exchanging emails and chasing attachments is a thing of the past with the Loan Participation Platform.

Too often the loan participation marketplace data is obscured by brokers who are looking to extract as much value as possible from credit unions for their own personal gain. At Alloya, we are accountable to credit unions. That's why we deliver transparent market data and insight to help our members make better-informed loan participation purchase and sale decisions.

RATES & SPREADS

As noted, Alloya's most recent *Economic Update*, we ended 2021 with COVID cases at an all-time high and inflation at its highest level in three decades. With elevated inflation as a backdrop, one would expect to see market rates rise. The 10-year Treasury ended approximately 30 basis points higher while the two-year ended 27 basis points higher. Both rates are important benchmarks for mortgage and auto loan pools, respectively.

Changes in market rates began to stabilize between Q2 and Q3 of 2021. The Treasury yield curve saw a modest decline over the period but still materially higher than the beginning of 2020. Spreads for loan participations have followed a similar trajectory. During Q1 of 2021, spreads continued to tighten as the market was largely dictated by sellers. During Q3, this trend began to stabilize, and we have seen spreads range from holding steady to modestly increasing. While we have seen increases in loan pool rates, the changes have been more modest than the changes in Treasury rates. This has resulted in a compression of spreads across asset classes and is indicative of the high demand seen for purchasing loan participations. Credit unions continue to have significant liquidity and loan participations continue to be an excellent value for putting that liquidity to work.

VOLUME

At year-end 2021, Alloya traded over $780 million on its Loan Participation Platform despite the lower-than-average loan volume in the industry. We continue to add new sellers to the platform, which now has over 20 active sellers, and are adding several more per month. If you are interested in purchasing loan participations, we encourage you to add your pool requests to the platform as many of these deals are allocated based on existing requests and never hit the open market.

LOSS & PREPAYS

Prepayment activity continued to see activity moderate in Q4 of 2021 relative to the earlier part of the year. Not surprisingly, an increase in rates has removed some of the incentive for consumers to refinance current borrowings. If inflation and market rates continue to increase, we would expect this trend to continue.

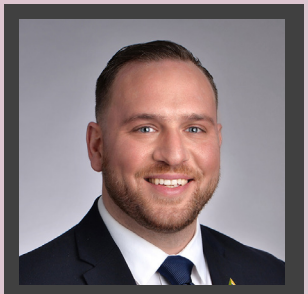
Subscribe to Receive Next Quarter's Issue

We hope you enjoyed the third edition of the *LP Quarterly* and will consider reading again when we release another edition in Q2. And remember, sharing is caring. Consider inviting a colleague to read the *LP Quarterly* and encourage them to subscribe so they receive the next issue straight to their inbox.

Visit **www.alloyacorp.org/subscriptions** to sign up.

THE 1 THING

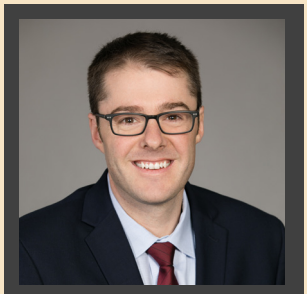
To close out every *LP Quarterly*, the Loan Participation team will share "one thing" they consider to be most important in the current state of the market.



BILL PATON
VP, LOAN PARTICIPATIONS & LENDING

BILL'S ONE THING

Consider availability your most important ally. Most credit union buyers are focused on sourcing auto loans because of their shorter maturity. The problem is that autos are few and far between in today's market due to a serious shortage of inventory from supply-chain issues. Rather than waiting around for a loan pool that may or may not become available, look at every deal that hits the market. You may not want to buy unsecured loans due to their perceived risk, or mortgage loans because of their longer maturity, but putting your money to work now is better than sitting around waiting. As always, consult with your Alloya Investment Services representative to determine suitability for your credit union.



RYAN McCARROLL
VP, LOAN PARTICIPATIONS

RYAN'S ONE THING

Consider spreads when analyzing loan participations. All too often we tend to look at the absolute value of an investment's yield when deciding where to employ excess liquidity. It is important to consider any investment, loan participations or otherwise, against your next best alternative. It is often the case that a loan participation has the best relative value available to credit unions, but this analysis should always be top of mind.

BRIAN MYERS
CONSULTANT, LOAN PARTICIPATIONS

BRIAN'S ONE THING

If you have not already submitted your pool requests on our Loan Participation Platform, we encourage you to do so. This allows you to specify the amount, loan type and any other requirements that you may have for a pool. The vast majority of our offerings are privately placed with buyers on this list. If you have not yet completed your requests, you may be missing out on loan participation opportunities. Feel free to email me at brian.myers@alloyacorp.org if you have any questions about this process.