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| Grander INVESTMENT mANAGEMENT, LLC | | |
| 2nd Quarter Summary and Outlook | | |
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This summary was prepared to provide our insight into our management of mortgage servicing rights (MSR) trends, performance, and market outlook.

**2022 Mortgage Market Conditions**

US interest rate markets were extraordinarily volatile in 2022, even by recent pandemic standards, with the 10-year treasury trading in a 250-bps range – the range itself being wider than the absolute level of the 10y to start the year. Rates peaked in early November at almost 4.25% before rallying to end the year around 3.75%. Both the absolute increase in rates of 225 bps YoY and the volatility resulted in a massive increase in the current 30y fixed rate mortgage coupon. Starting the year around 3.25% - deliverable into 2.5 par coupon MBS securitizations – rates peaked in early fall, actually before the peak 10y Treasury rate, at over 7.5% for the average conforming offer rate – rates not seen since 2009. Importantly, the last time rates were that high, substantial portions of the conforming eligible housing market still had some refi incentive; FHLMC now estimates that less than 2% of homeowners, representing less than 1% of total US mortgage balances, have a refinancing incentive at current levels. Moreover, rates are not coming down, with conforming rates still caught in a range around 6.5% to 7.0%. The curve inversion and rapid increase in Fed Funds rates has also eliminated a tradition rate management vehicle seen in past rate cycles, the flip into 3/1 and 1/1 ARM product. With the 3m-10y spread at -100 bps as of early January, ARM products are even more expensive than 30y conforming product. *The result*: a massive extension of MBS duration across all pre-Q1 2022 vintages, as prepayments cratered. Some 2022 on the run pools are seeing prepayment rates lower than what would typically be experienced due to home sales and “life events” as borrowers seek to hold onto the last vestiges of “free money” in the mortgage market for as long as possible. Home sales have dropped – still, however, largely due to supply issues – as new home affordability has become more challenging for borrowers.

**2022 MSR Performance**

GIM’s initial purchase funded a pool of servicing rights from mostly 2020 vintage loans with a weighted average coupon (WAC) of 2.74%, one of the lowest WAC pools that traded in 2021. We anticipated slower prepayments than average, but as current coupons soared, prepayments fell to the lowest I’ve seen in my career, including September and October in which the number of payoffs was in the low single digits within a 4000-loan pool. The result was a massive extension in expected cash flows, and a resulting markup on the market value of the pool. While we are still calculating final YE returns, performance for 2022 was driven both by greater than expected cash flow from slow prepayments, and more significantly, from an almost 30% increase in expected NPV of future cash flows due to the extension. Note significantly that we do not expect this performance to be repeated in 2023, but we also see no signs of giving back any of the valuation adjustments, as the low WAC of our pools remains nearly 400 bps in the money to borrowers, and home price appreciation in our core US Southeast and Midwest markets largely do not enable home “flipping” into newer, much higher coupon mortgages and house prices. We expect 2023 performance to be solidly in the 10-12% range, in line with our pricing of the original pool purchases in 2021 and 2022, but on a higher valuation basis due to the market “adjustment” which occurred in our favor in 2022.

**2023 Trends**

MSR valuations have largely been shocked, and market activity has been muted as a result. For those servicers who had purchased servicing on the pre-2022 low WAC origination vintages, valuations have been friendly, and it has alleviated pressure on non-bank servicers as the higher valuations allow for greater advance rates on leverage facilities. Grander’s acquisition model, however, *is focused on bank originators who acquire MSRs via retail loan origination in their branch and local footprints.* Banks are preparing for potential recession conditions in 2023 and 2024 and for potential losses in core commercial real estate markets, where pandemic disruptions to office and retail portfolios continue to roil both valuations and forward project activity. These midsize and smaller banks see the increase in the value in their MSR portfolios as a double-edged sword: while obviously being attractive economically, by growing in value they require more Tier I capital to support the asset. Thus, selling the MSR to a friendly buyer who *does not* want to acquire the customer or compete in other bank products becomes a particularly attractive capital source to these banks, and in our conversations, we see this dynamic playing out actively in 2023.

**Portfolio Stratification as of 3/31/23**

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Description automatically generated with low confidence

**What are Mortgage Servicing Rights (MSR)?**

A mortgage servicing right is the right to service a loan on behalf of an investor and collect a servicing fee. Loan servicing consists of collecting and processing loan payments throughout the life of a loan. Servicing activities also include billing the borrower; collecting principal and interest payments as well as taxes and insurance payments; disbursing property taxes and insurance premiums; accounting for these activities at the loan and investor level; and forwarding funds to an investor in the secondary market. MSRs are a modified interest-only strip. The expected life of the loan is calculated based on its expected prepayment rate and is a key valuation variable.

**About Grander**

Grander was founded in 2017 out of the collaboration of two forward thinking entrepreneurs, Robert Williams, and Curtis Whitaker. Combined they bring 60 years of banking and capital markets experience with the goal of delivering consecutive and compelling returns in Mortgage Servicing Rights (MSR) space. Grander’s investment strategy are managed by dedicated and seasoned team focused on Mortgage Servicing Rights. Investment decisions are driven by our disciplined research and due diligence process. We pursue unique sourcing of MSR’s to deliver investment opportunities to our clients that are not readily available to the broader markets. Through our disciplined and comprehensive research process and risk management, we seek to generate compelling risk adjusted returns. Established as a master servicer, Grander has secured state and federal license authorization. Grander is licensed in all but three states as a master servicer and is an “approved” seller servicer for Freddie Mac loans. In the process of obtaining approval as master servicer for Fannie Mae loans and eventually attaining Ginnie Mae approval.

# Please contact your Grander representative for additional information or to answer any questions.