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PRESENTATION

Operator

Good day, and welcome to the Flagstar Bank First Quarter 2020 Earnings Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Ken Schellenberg, VP, Investor Relations. Please go ahead, sir.

Kenneth Schellenberg - *Flagstar Bancorp, Inc. - VP of IR*

Thank you, Michelle, and good morning. Welcome to the Flagstar First Quarter 2020 Earnings Call. Before we begin, I'd like to mention that our first quarter earnings release and presentation are available on our website at flagstar.com. I would also like to remind you that any forward-looking statements made during today's call are subject to risks and uncertainty.

Factors that could materially change our current forward-looking assumptions are described on Slide #2 of today's presentation in our press release and in our 2019 Form 10-K and subsequent reports on file with the SEC. We are also discussing GAAP and non-GAAP financial measures, which are described in our earnings release and in the presentation we made available for this earnings call. You should also refer to these documents as part of this call. With that, I'd like to now turn the call over to Sandro Dinello, our President and Chief Executive Officer.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Thank you, Ken, and good morning to everyone listening in. My apologies for the delay in getting this going today. And unfortunately, our conference call company is having some difficulties. I don't think it has anything to do with all of us being remote. So hopefully, the rest of this [calls] are much smoother than it has thus far. And I hope that all of you, and your loved the ones who have been able to stay safe and healthy. And as I said, in the spirit of proper social distancing, I'm joined remotely this morning by Jim Ciroli, our Chief Financial Officer; Lee Smith, our Chief Operating Officer; Kristy Fercho, our President of Mortgage; and Steve Figliuolo, our Chief Risk Officer.

I'm not going to spend much time today on our results, except for some commentary on our provision. I think it's more important to tell you how we've adjusted our operations in the face of COVID-19 and how I think we'll operate going forward given the uncertainty of the length of this pandemic. With respect to our results, it was a strong quarter with earnings of $0.80 per share, stronger still if you look at our pre-provision net revenue. Details will come from Jim and Lee in their remarks.

So let me start with some comments about our position, which totaled $14 million for the quarter. Admittedly, the provision for the quarter was difficult to estimate. We had no option but to use an immature model to estimate life of loan losses in perhaps the most uncertain economic time in our history. And when you add the unknown impact of government assistance programs to the mix, it was a daunting endeavor. Frankly, I don't think that there is a model that exists that can accurately predict the life of loan loss at this stage of the game.

That said, based on our current data, we're comfortable with our analysis. We have a strong commercial portfolio that, at the end of the quarter, had no nonperforming loans. And thus far, we've seen more weakness. As you know, our portfolio is diversified with no outsized exposure to any geography or industry including little exposure to the auto industry.

Our loan concentration policy is highly granular and conservatively structured, built to be resilient to a recession. Now we find ourselves in a recession, perhaps a deep one that may linger for the next 18 months. A hallmark of our lending philosophy has been to bank only proven operators. And the eleventh commandment of Flagstar is that's thou shall not lend to anyone that has walked away from a bank obligation. These principles, coupled with the fact that virtually all our borrowers are recession-hardened will help mitigate credit concerns going forward.

Finally, I'll remind you that while we're a $27 billion bank in terms of assets, our commercial credits, net of warehouse loans, total less than $5 billion. Thus far, every borrower is working with us. And to date, they are all positive about their ability to weather the storm and remain a growing concern. Thus far, 252 commercial borrowers representing $548 million in unpaid balances, just 11% of our commercial book have requested payment deferrals and all were in good standing prior to their request. Business banking requests account for $71 million, with C&I and CRE representing $287 million and $190 million, respectively. It's worth noting that we received no deferral requests from our homebuilder clients thus far.

We are on top of every one of our credits, both monitoring and actively managing for the slightest work. We have assisted many of these customers with a PPP loan, and we will be assisting even more through the Main Street Lending program. We're being careful in connection with new commercial loan requests outside of our warehouse business, and we are pulling back on commitments wherever it's prudent and the opportunity presents itself. Even inside warehouse lending, we've taken a more conservative approach. Essentially accepting no-jumbo or non-QM loans as collateral and requiring a tighter credit box for government loans and lower advance rates for loans that we believe are at higher risk.

As to our consumer loan portfolio, we consist largely of low-LTV, high-FICO mortgage loans and high FICO of HELOCs. Thus far, we've seen no material weakness in those loans. I think it's a given that the economic forecast at June 30 will be weaker than those at March 31. So I fully expect that our ACL model will suggest a significant allowance adjustment for Q2, but just how much is impossible to predict.

My opinion is that GDP will contract perhaps as much as 10% in Q2. So as much as 40% on an annualized basis, followed by a slow growth in the ensuing quarters. Unemployment might reach 20% in Q2, then gradually declining as GDP improves. So not quite what I would call it the recovery. I realize this opinion is probably on the pessimistic side of the universe of thinking, but my view is that it's most prudent to prepare for the worst and hope for the best, and that's exactly what we're doing.

Next, I'd like to speak to how our company responded to the pandemic, and I'll start by saying I could not be more proud of our team and how we've adjusted. We could not have gone much better. We prepared for a possible pandemic in our business continuity plan. As part of that plan 3 years ago, we've moved a vast majority of our people to laptops. Additionally, we have secured enough VPN licenses and bandwidth to move quickly. And so the transition went really well. Today, over 80% of our employees are working remotely. And interestingly, productivity has not dropped.

In fact, in the last 2 weeks of the month, we processed over $2 billion of mortgage loans, increased warehouse balances by over $1 million -- $1.5 billion; worked out arrangements with every commercial customer seeking a deferral; accepted thousands of requests for mortgage forbearance; and built a new technology platform, literally overnight, to launch the Paycheck Protection Program and got it up and running 36 hours after the guidelines were released. We took and processed over 3,000 applications for $400 million in loans.

Remarkably, all these processes were performed and managed remotely. Additionally, on March 16, we eliminated in-branch service at select bank branches, and then a few days later, moved to drive-up service only with lobby access by appointment and not one customer complaint has reached my desk. In fact, deposit growth has been encouraging. We reduced rates aggressively following this Fed move and still saw deposit balances increased about $900 million during the quarter. And we've seen a further increase in deposits in April of over $350 million from our banking customers. While I don't know when normal will return or what it will look like, I can tell you we will be very conservative in moving people back to our facilities. That's the right thing for our team. And given how smoothly we are operating, there's no need to get ahead of a clear flattening of the curve.

As always, we've always been there for our communities. To date, we've contributed almost $600,000 in markets across the country to support the COVID-19 cause, including $300,000 to a cotton silk company that shifted to manufacturing masks that are being donated to hospitals. Only 17 of 4,700 Flagstar employees and contractors have tested positive for COVID-19, and best of all, they all have either recovered or appeared to be on the road to recovery.

We believe that's, in large part, because we started our social distancing early on March 13. Also very please to tell you that we surveyed our team and 98% felt that Flagstar responded effectively to both emlpoyee and customer-related concerns. As difficult as the last 6 weeks have been, I do think we retain the resilience of our business model in action. Here's why: First, I think we can sustain net interest income on the back of our warehouse business, which currently has outstanding balances of approximately $3.8 billion, with a month-to-date average balance of over $4 billion. Warehouse lines are now almost entirely secured by conforming agency and government products. The portfolio provides strong returns with virtually no credit risk, and 91% of these loans had rate flows. We've been without booking new commercial loans outside of warehouse, we expect to grow net interest income.

Second, the mortgage business continues to be strong. Our gain on sale month-to-date is over $90 million and shows no signs of weakening with over 95% of the lots representing conforming agency loans. While I want to opine on how long this performance will continue, I think it demonstrates the power of this business in the current environment. While we're not guiding on net interest income or lock-switching one, in Sallie Mae's most recent projection of a 10% increase in originations for 2020 as compared to 2019 holds true, our warehouse and mortgage businesses will thrive, and we will be in a position to build a credit war chest without the pin into capital should it be needed.

To put it mildly, giving guidance right now is too much desperate. However, I believe Flagstar is well positioned to weather the storm and come out stronger on the other side. Our profitability is strong, our capital is strong, our allowance is strong, our liquidity is strong and our business model was working precisely as we designed it.

Finally, I'd like to make it clear that we don't expect to change our dividend posture in the near term, and we're not contemplating stock buybacks at this time. Obviously, my comments today have been unlike anything before because we are in unprecedented times. My goal has been to give you my perspective on how I see Flagstar performing in the near future in the context of the SEC's recent guidance and safe harbor protections. In doing so and drawing on more than 40 years of experience at Flagstar and a deep understanding of the company and the quality and caliber of its employees, we are committed to doing the right thing for our employees, customers and our communities.

Protecting their health will secure Flagstar's health. We will focus on the opportunities this environment gives us, and though we will continue to manage the risks we face conservatively, we will not dwell on them. If we do that, I firmly believe we will produce the best possible results for our shareholders. With that, I'll turn it over to Jim.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Thanks, Sandro. Turning to Slide 7. Our net income this quarter was $46 million or $0.80 per share. This performance compares to the $58 million or $1 per share last quarter. The decline on a linked-quarter basis was largely due to the $14 million credit provision this quarter. We had adjusted net income of $37 million or $0.64 per share in the same quarter last year.

Diving deeper into this quarter's performance. Our pretax pre-provision earnings were $70 million this quarter compared to $69 million last quarter. Net interest income was down $4 million or 3% over the prior quarter. Average earning assets grew $442 million.

In line with our expectations, the net interest margin decreased by only 10 basis points despite 150 basis points of rate cuts in March that were unexpected. This performance was driven both by our strong core deposit franchise, consisting of granular retail customers and by a well-positioned, well-diversified loan portfolio that has a large composition of fixed rate assets and floors on many of its variable rate loans. We'll review these numbers further on the next slide.

Mortgage revenues were $96 million, a decrease of $2 million or 2% compared to the prior quarter. During the quarter, we saw gain-on-sale margins increased significantly as primary, secondary spreads widened to historic levels and lenders work to manage capacity. However, in the second half of March, extreme market dislocation and volatility occurred, and we experienced $45 million of hedge losses, which I'll discuss further in a moment.

Asset quality remained strong. Net charge-offs were 8 basis points, and nonperforming loans were relatively flat to year-end. Our allowance for credit losses, or ACL, which includes the reserve for unfunded loan commitments, was $152 million at quarter end, up from $110 million at year-end. At these levels, our coverage of loans, HFI, is 1.5%. This was the result of our January 1 CECL adoption and the $14 million credit provision this quarter. We'll provide more details when we get to the asset quality slide and take a deeper dive into CECL.

Capital also remained solid. Despite our balance sheet ending the quarter at $27 billion, up from $23 billion at year-end, all capital ratios remained above the stress buffers that we've established based on our DFAST models. Total risk-based capital was 11.2% at March 31. Our CET1 ratio was 9.2%, and our Tier 1 leverage ratio was 8.1%. We'll go into more details on capital later, so let's turn to Slide 8 and dive deeper into the income statement.

Net interest income decreased $4 million to $148 million this quarter, which was 3% lower than last quarter. Nearly half of this decline resulted from having 1 less day in the quarter. The results reflect the 2% increase in average-earning assets led by investment securities, loans held for sale and commercial real estate loans. Deposit costs came down 9 basis points, while average deposit balances were relatively flat quarter-over-quarter, excluding a decline in broker deposits. We'll dive deeper into net interest income and our interest rate risk addition on the next slide.

Noninterest income decreased $5 million or 3% to $157 million due to lower mortgage revenues. Our gain-on-sale revenue was $90 million, representing a decrease of $11 million or 11% from the prior quarter. Fallout-adjusted LOCs increased 36% to $11.2 billion. And the gain-on-sale margin decreased to 80 basis points. Channel margins were strong, especially in our delegated bulk channel.

The Fed's buying of mortgage-backed securities beginning on March 16, pushed prices on MBS much higher. This price change impacts the values of the TBA mortgage-backed securities that we sell short to hedge our pipeline and closed loans held for sale. As the pipeline in closed loans did not experience the same level of price appreciation, the short position declined in value more than the long position increasing value, creating $45 million of hedge losses. We've added Slide 40 in the appendix to provide more details on what we and the industry experienced.

We were reacting quickly to this phenomenon, took actions to rebalance our hedge profile. And made pricing changes, which improved our position by month end. In April, the Fed modified their purchases and our actions took hold, which stabilized our gain on sale. Through last Friday, we recorded over $90 million of gain-on-sale revenue for April. While we won't forecast what the second quarter gain on sale revenue will be, this partial-month result indicates that the hedging issues have not persisted. We also had a $9 million improvement in the MSR return. The result of hedging gains this quarter. Loan administration income improved $4 million due to higher average loans serviced and a decline in the LIBOR-based credit that we provide to our subservicing customers for the custodial deposits that they control.

Noninterest expense was $235 million, down $10 million from the prior quarter. The decrease was primarily related to $5 million of balance sheet cleanup and discretionary expenses that took place in the fourth quarter and did not recur. Expenses were also down as mortgage loan closings declined 8%. Overall, mortgage expenses as a percentage of closings were consistent with the prior 2 quarters. Lee will provide more color on expenses later.

We've added Slide 9 to provide more details on our interest rate risk position at the end of the quarter. While we won't provide guidance on net interest income, we feel that we're in a good position. Looking at our commercial loan portfolio, 95% of the loans are variable. As we parse that variable percent out, as Sandro mentioned, over 90% of our warehouse loans have floors in them. We also have floors in many of our C&I and CRE loans, either floors that don't allow LIBOR to reset below 0 or floors with LIBOR at a higher level. Consequently, we don't see a lot of risk-to-spread compression coming from the asset side of the balance sheet.

Looking at deposits, we have moved pricing down on our portfolio in reaction to the aggressive actions taken by the Fed to drive short-term interest rates. At quarter end, in the retail CD book, we had $1.8 billion of CDs that mature in the remaining 9 months of this year and reset to lower rates. We also had $900 million of savings and money market accounts at quarter end. So we're under some level of promotional rate that will come off that promotional rate, which has an average cost of 1.9% and also repriced lower in the latter part of this year. Approximately 85% of our custodial deposits are controlled by our subservicing clients and naturally priced down as those rates are based on LIBOR.

In summary, we believe that the deposit rates could be a tailwind for the remainder of the year. Also on the liability side, we've executed interest rate swaps and entered into long-term FHLB advances to lock in lower rate funding, lathering those out between 3 and 7 years. We've now executed $1.5 billion of this strategy, securing long-term funding at an average cost of 61 basis points, well below our cost of funds in Q1.

While it's difficult to predict where rates might be for the remainder of this year, we feel that our interest rate risk position is in a good place, especially considering the liability-sensitive nature for mortgage business. We feel that we can protect our net interest income and net interest margin in this environment. And believe that our net interest margin should be relatively flat to the first quarter. This perspective also contemplates the impact of the PPP loans that we have originated under deferral of the FDIC on those loans. To illustrate how it's positioned us, I would share that while the first quarter net interest margin was 2.81%, March's net interest margin was 2.84%, showing the effectiveness of the actions we've taken to protect net interest income.

Let's turn to Slide 10, which highlights our average balance sheet this quarter. Average loans held for investment declined $0.3 billion, driven by a decrease in average warehouse loans and residential first mortgages. Most of the decline in warehouse was seasonal and the decrease in average residential mortgages was the result of loan prepayments. At quarter end, we saw higher levels of warehouse loans and loans held for sale.

The higher levels of warehouse loans resulted from our actions to continue to support customers in the mortgage finance business, even as we took a more conservative approach with non-QM and jumbo loans, and tighten the credit box and the government loans that we will support on our warehouse lines. For loan held for sale, we saw elevated levels of newly created mortgage-backed securities that could not be sold at reasonable prices due to supply imbalances in the market. Ultimately, we delivered these bonds into our TBAs in April. While this inflated our balance sheet and compressed our spreads a bit, we were able to hold these assets without sacrificing execution.

We expect that we'll continue to have relatively higher balances in our warehouse and mortgage loans held for sale portfolios in the second quarter. Average deposits decreased $0.1 billion, driven by lower CD and wholesale deposit balances. Higher demand deposits partially offset this runoff. We continue to have a strong liquidity position, driven by the strength of our deposit base and access to multiple sources of liquidity, both on balance sheet with our high-quality securities portfolio and off-balance sheet with our undrawn FHLB facilities. We also plan to fund our PPP loans using the Fed's PPP facility and have ample access to borrow at the discount window.

Finally, we continue to demonstrate significant capital generation capabilities with growth in our tangible book value per share of $29.52 at quarter end, up $0.95 from year-end.

Let's turn to asset quality on Slide 11. Credit quality in the loan portfolio remained strong. Delinquencies continue to be relatively low. Only 40 basis points of total loans were over 30 days delinquent, up 7 basis points from year-end. Our allowance for credit losses covered 1.1% of total HFI loans. This coverage now includes our reserve for unfunded loan commitments.

Excluding warehouse loans for the denominator, given their relatively clean credit loss history and considering that substantially all of these are collateralized as agency and government-backed loans, our coverage ratio would stand at 1.5%, consistent with what we see other banks having under CECL.

Considering the economic uncertainties related to COVID, we're monitoring our entire loan portfolio doing additional analyses within certain sectors and relationships and staying in close communication with our significant borrowers.

On Slide 12, we wanted to share with you our exposure to those industries that we believe are more likely to be most impacted. In total, we have just under $1 billion of outstanding loans in this category, representing only 7% of our loan portfolio. In the commercial loan portfolio, these balances totaled $328 million. Within this group, we're focused on our exposures to automotive, hospitals and leisure and entertainment businesses, which includes restaurants. You can see that the exposure here is relatively low. We have no oil and gas exposure.

In our commercial real estate portfolio, we have $647 million outstanding in the areas most likely to be impacted by COVID, including loans secured with hotels, retail properties and senior housing. Of the loans in this category, our average LTV is 55%, and our average debt service coverage was 1.6x. We'll be analyzing all of our borrower relationships this quarter. While we know this will be a challenging time for many people, we believe that our low level of exposure to these industries is the result of our well-diversified loan portfolio and the strong LTV and debt service coverage ratios, the result of our credit discipline.

So let's turn to Slide 13. We wanted to walk you through how we implemented CECL, how we got to the CECL balance at the end of the quarter and how we'll be thinking about CECL in light of the uncertain economic outlook that we have right now.

Overall, we ended the quarter with $152 million allowance for credit losses, consisting of $132 million of allowance for loan losses and $20 million in the reserve for unfunded loan commitments. The reserve for unfunded loan commitments is included in other liabilities on our balance sheet. Both are available to cover credit losses in the loan portfolio. In total, our allowance for credit losses at quarter end represents a 38% increase over what we've reported at the end of 2019.

In our adoption of CECL, we use 3 different forecasts of the next 2 years, which then reverted to a long-term average over a 1-year period. These forecasts included an adverse projection that reflected severe economic distress. We weighted that model 30-day -- 30% in our day 1 adoption. Our quarter-end estimates, we elected to use the March 27 Moody's baseline, which reflects the economic distress caused by COVID and also contemplates some impact that the government actions taken to mitigate the stress. The forecast assumes that we are in a sudden sharp and severe recession, only partially recovering later in the year.

In this scenario, GDP contracted 18% in Q2 and HPI decreases 3% by the end of the year and unemployment spikes to 9% and moderates to 7% by the end of the year. We also judgmentally increased reserves in our CRE, homebuilder and C&I portfolios to provide additional coverage for industries and customers that we thought could be more exposed to the stressful conditions in our forecast. We've provided a portfolio-by-portfolio breakdown of the resulting ACL coverage ratios in our appendix. We also continue to maintain reserves for our loans with government guarantees and specifically measured loans whose amounts are not impacted by the CECL methodology change. Finally, as you'd expect, we've elected to defer the regulatory capital impact of adopting CECL until the end of 2021, after which it will be phased in at 25% per year.

Turning to Slide 14. Despite tremendous balance sheet growth, our capital ratios remained solid and nicely above our stress buffers. Total risk-based capital was 11.2% at March 31, down only 31 basis points while our CET1 ratio of 9.2% was relatively unchanged. Our Tier 1 leverage ratio of 8.1% actually increased 9 basis points at the same ratio pro forma with capital simplification as this ratio is based on average balances and the balance sheet growth and loans held for sale and warehouse loans happened toward the end of the quarter. I'd expect our Tier 1 leverage ratio to be lower next quarter.

Between loan book for sale and our warehouse loan portfolio, we have approximately 540 basis points total risk-based capital and over 400 basis points of Tier 1 leverage capital dedicated to these 2 asset categories that have very low-risk content.

In warehouse lending, which has 100% risk rate, we've had under $5 million of losses cumulative for the last 12 years, and we took a more conservative approach during the quarter for certain product categories. I'd remind you that we also hold the collateral for those loans, while they are on our lines, and that collateral consisted almost entirely of agency and government-backed loans. Loans held for sale also had very little risk content and over $2 billion of these balances at quarter end were Fannie, Freddie or Ginnie securities and were reflected in our trading portfolio.

In summary, we believe that we're operating at strong capital levels, given our low-risk balance sheet composition as more than half of our assets at quarter end were in categories that have very low-risk content. That is loans and trading securities held for sale, warehouse loans, investment securities, loans with government guarantees and cash.

I'll now turn to Lee for more insight in each of our businesses.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO of Flagstar Bank*

Thanks, Jim, and good morning, everyone. We're very pleased with our net income of $0.80 per diluted share for the first quarter, which increased tangible book value to $29.52, but more importantly, I couldn't be more proud of how we've responded as an organization to the COVID-19 pandemic. Nothing is more critical than the health and safety of the Flagstar family. And we were able to pivot quickly and ensure the vast majority of our employees were working from home by Monday, March 16.

This didn't just happen. We conducted a 2,500 employee remote work test on Friday, March 13 and expanded our network capacity in the days leading up to stay-at-home orders being put in place, which increased our remote connection capacity by 10,000 users. For those employees still needing to work from Flagstar facilities, we moved to implement distancing standards, an enhanced cleaning regimen and provide necessary protective equipment to ensure they felt as safe as possible while on site. It's testament to the morale and spirit of the Flagstar team that during this transition, we didn't miss a beat and continued to serve our customers and partners with the same exceptional standards they've come to expect from us.

As government relief programs have been rolled out, we've moved quickly and efficiently to ensure our customers can participate and benefit. We took over 3,000 applications for the Paycheck Protection Program and have worked with thousands of borrowers requesting forbearance relief on their mortgages. We've increased our call center capacity and have not seen material wait or hold times throughout this period.

Furthermore, there has been no layoffs or furloughs at Flagstar. A lot has been thrown at us over the last 7 weeks, but the team has stood tall. And I believe the journey we've been on over the last few years, including the multiple acquisitions, has helped prepare us for this moment. Now more than ever, I believe our business model will shine.

We previously talked about how our different business lines act as a natural hedge. And in this low interest rate environment, mortgage originations, because of increased refinance volume, has performed exceptionally well, so as our warehouse lending. And these 2 businesses have been well supported by our subservicing operation. 52% of our revenues in the first quarter were from noninterest or fee income business, and I believe this deliberate and well-balanced mix will ensure continued strong performance as we move forward.

There were several other notable developments during the quarter, which included: average interest-earning assets increased $442 million or 2%, primarily a result of an increase in investment securities, while our net interest margin decreased 10 basis points to 2.81% as we effectively manage net interest margin compression through timely and thoughtful actions on the liability side of the balance sheet; we adopted CECL, increasing our credit reserves to $152 million at the end of the quarter, $18 million of which was the result of COVID-19 and its potential impact on our loan portfolio in the future; we maintain a diversified lending portfolio with quality credits and no significant exposure in any one industry; mortgage banking revenues decreased only $2 million or 2% to $96 million in the first quarter versus $98 million in the fourth quarter as we continue to take advantage of the strong refinance market; our subservicing business remained relatively flat in terms of loans serviced or subserviced. And at the end of March, we were servicing or subservicing approximately 1.1 million loans, which generates consistent noninterest fee income for the bank.

For the fifth consecutive year, we were awarded the Fannie Mae STAR Performer Award in general servicing, which is testament to the exceptional work and commitment of our servicing, call center and collections teams.

Finally, our capital position remained solid, and we maintained strong liquidity, particularly given our broad deposit base and our access to Federal Home Loan Bank funding, which means we're well positioned to not only weather this pandemic, but also support our customers and business partners who are not so fortunate.

It's undoubtedly been a thrilling time, but we've rallied exceptionally well as an organization as a result of our fantastic employees, team-oriented approach and robust business model.

I will now outline some of the key operating metrics from each of our major business segments during the first quarter.

Please turn to Slide 16. Quarterly operating highlights for the Community Banking segment include average commercial and industrial and commercial real estate loans increased $127 million or 3%, with the growth being driven by the CRE lending group. We've been actively managing our commercial loan portfolio since the advent of COVID-19 and working closely with our customers given our relationship-based approach.

Line of credit usage increased from 49% to 60% or $249 million between March 13 and April 17. We continue to be thoughtful in terms of new facilities and believe our strong credit policies and diversified portfolio will be a strength as the fallout from this pandemic becomes more apparent. Average consumer loans held for investment decreased $35 million or 1% of as we ended the quarter with approximately $4.9 billion of consumer loans on our balance sheet, with 82% being residential first lien mortgages and HELOCs.

Through April 24, we have received approximately 2,000 requests for deferrals on our nonmortgage consumer loan portfolio, which amounts to $119 million or 5.8% of all outstanding balances. Utilization levels on HELOCs have remained fairly flat throughout the pandemic period. I will talk about forbearance activity on first lien mortgages shortly.

Average warehouse lending loans decreased $437 million or 16% to $2.3 billion in the quarter due to fewer days online resulting from the seasonal slowdown in mortgage activity, particularly in January and February. However, we made changes to our warehouse credit box at the end of the quarter as a result of the volatility in the mortgage market. We honored all loans that were on the line at the time of announcing, we were going to stop financing non-QM and jumbo loans. Furthermore, we tightened our FICO limits around several other products in response to the market uncertainty and to protect our own position.

I would add that during the month of April, we have been encouraged to see continued high outstanding average balances in warehouse lending. And given its positive correlation to the mortgage business, it acts as a nice hedge in a low interest rate environment when refinance activity is thriving. Overall, this means average loans held for investment decreased $345 million, which drove the $4 million or 3% decrease in net interest income quarter-over-quarter. In order to help our customers, we participated in administering the SBA's Paycheck protection program just after the quarter ended and received approximately 3,000 applications, totaling approximately $400 million.

This program was introduced very quickly, and the Flagstar team did an outstanding job of standing this up and ensuring our customers were able to participate and benefit. 150 of our 160 bank branches remain open. The 10 that are closed do not have a driver and are located in close proximity to another branch, so we chose to close them to further protect our employees.

All of our ATMs remain operational. Average deposits, which include all interest-bearing and noninterest-bearing retail and custodial accounts decreased approximately $100 million, but we did reduce the cost of interest-bearing deposits 13 basis points during the quarter as we moved quickly to compensate for the lower interest rate environment. We will continue to maintain our disciplined and relationship-based approach within the community bank. We feel we have a loan portfolio with strong credit qualities, and we'll continue to work closely with our customers throughout this pandemic.

Please turn to Slide 17. Quarterly operating highlights for the mortgage origination business include: fallout-adjusted lock volume increased 36% to $11.2 billion quarter-over-quarter while the net gain on loan sale margin decreased 43 basis points to 80 basis points. As a result, gain on sale decreased $11 million to $90 million in the quarter. The increase in fallout-adjusted lock volume was driven by the robust refinance market due to low interest rates, particularly during the month of March. Refinance activity accounted for 64% of our lock volume during the quarter.

Mortgage closings were $8.6 billion in the first quarter, an 8% decrease from the fourth quarter due to the anticipated seasonal slowdown in purchase market. The big story happened towards the end of the quarter, where we incurred a substantial loss on our pipeline hedge for the reasons Jim has previously described. This reduced our margin for the quarter materially but it was a short-term phenomenon and the hedge volatility settled down right after quarter end and has been stable during the month of April.

Similar to what we did on the warehouse side, right around quarter end, we moved to stop originating higher-risk products and tighten the credit box in certain areas to protect our position and minimize any future write-downs or losses. Despite moving to a work-from-home environment, our mortgage operations team continues to excel and keep up with the additional volume. We have not seen any degradation in productivity levels, and I believe this is due in large part to our underwriting staff being 98% remote prior to COVID-19. This means the shift in work environment wasn't unfamiliar.

Furthermore, we have not been affected by offshore shutdowns as almost all of our operations are here in the U.S. We continue to run a compliant and efficient operation of scale. We're pleased with how we reacted quickly at the end of the quarter to protect our mortgage earnings, both now and in the future and are very encouraged by what we've seen during the month of April. We have already booked over $90 million of gain-on-sale revenue through April 23. Mortgage has always been a key component of our business model and strategy. It generates significant noninterest fee income for the bank and is a natural hedge to some of our other businesses in a declining interest rate environment.

Moving to servicing. Quarterly operating highlights for the mortgage servicing segment on Slide 18 include: we ended the quarter servicing or subservicing approximately 1.1 million loans, of which over 917,000 or 85% of subservice for other MSR owners. Of the 1.1 million loans we've serviced or subserviced, 94% are backed by Fannie Mae, Freddie Mac or Ginnie Mae. The number of loans serviced to subserviced remained relatively flat in the quarter despite the high levels of refinance activity as we are able to replace runoff with new loans from our mortgage origination business.

Today, we have the capacity to service or subservice 2 million loans as well as provide ancillary offerings such as recapture services and financing solutions to MSR owners. Those offerings are proving to be very beneficial in this current environment.

If you look at Slide 39, you will see that we are achieving our $4 million to $6 million of operating profit before tax guidance for every 100,000 loans we add to the platform. The major issues for servicing right now are forbearance activity and liquidity. Through Thursday, April 23, 110,325 borrowers representing 10.7% of the portfolio that we either service or subservice have requested forbearance relief because of COVID-19. Interestingly, 50% or half of those borrowers have made their April payment and not taken advantage of the forbearance option. This effectively means that right now, 5.3% of the loan book we service or subservice is actually in forbearance.

As part of the forbearance period, we're also waiving certain fees, and there will be no negative reporting to the credit bureaus. As you may recall, we acquired a default servicing operation in Jacksonville in September 2019 in order to leverage our industry-leading oversight and monitoring and bring default servicing back in-house. Operationally, we couldn't have been better prepared to handle the spike in core volume because of this pandemic.

We have been monitoring call wait times closely and have been quick to react to the spikes to ensure we operate within our 1 minute average speed-to-answer service level requirement. Furthermore, we've set up a hardship relief task force within our default servicing team to proactively reach out to borrowers in forbearance and work out an appropriate loss-mitigation solution after they exit forbearance. This will streamline the operation and allow us to get ahead of things rather than just letting these loans run through the normal process.

During the quarter, we sold $6.6 billion of MSRs, $2.2 billion via bulk and $4.4 billion via flow sales and retained the subservicing on 85% of these sales. However, right now, there is no market for MSRs, given the recent market volatility and uncertainty surrounding liquidity on the advances. We do believe the market for MSRs will come back in the near future. But in the meantime, we're very comfortable retaining the MSRs we create through our origination business on our balance sheet. Our MSR to CET1 ratio is currently 13.6%, so we have plenty of room before we start to approach the 25% MSR to CET1 capital level and intend to use the runway we created through the end of the year, if necessary.

Of the 1.1 million loans we service or subservice, only 9% are MSRs Flagstar owns. It's a small percentage on the liquidity need on the advances is immaterial, given our overall strong liquidity position as a bank. Finally, custodial deposits averaged $4.8 billion in the first quarter, which was flat compared to prior quarter. Again, this is just one additional benefit we get from our subservicing business as it provides liquidity that helps fund our balance sheet.

Now more than ever, the strength of our subservicing business within a bank that is well capitalized and has plenty of liquidity stands alone in the industry, and I expect you will continue to see it thrive in the future.

Moving on to expenses on Slide 20. Our total noninterest expenses decreased 4% or $10 million to $235 million quarter-over-quarter, and total revenues also decreased by $10 million to $305 million. Generating positive operating leverage of 1.4% in the quarter. The main driver of the decrease in expenses was lower mortgage closings.

If you look at Slide 21, our core non-mortgage noninterest expenses were $139 million in Q1. Within this amount is a onetime write-off of $2 million, which relates to a 2013 legacy sale, meaning the run rate is $137 million, a slight increase of $1 million from last quarter. Expenses tied directly to the mortgage origination business were $96 million, a decrease of $8 million versus Q4, given mortgage closings which drive mortgage expenses, were down 8%. As a percentage of mortgage closings, mortgage expenses have been very consistent for the last 3 quarters, as you can see on Slide 21. Our efficiency ratio was 77% for the first quarter, which was an improvement of 1% from the prior quarter for the reasons I've just outlined.

Given the uncertainty around the mortgage market and COVID-19 expenses, we will not be providing Q2 noninterest expense guidance at this time. It's an unprecedented time on the health and safety of the Flagstar family, our employees, customers, partners, communities and stakeholders is our #1 priority. The way the team has adapted to this new environment without breaking stride has been exceptional. We will continue to work relentlessly to help our customers through this difficult situation, and we will come out the other side stronger for it. I believe the strength of our business model and logic of our business strategy will prevail in this uncertain environment.

This concludes our prepared remarks, and we will now open the call to questions from our listeners.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we'll first hear from Scott Seifers with Piper Sandler.

Robert Scott Siefers - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

I guess, first question I wanted to ask is just on that increase in the trading securities of about $2.1 billion, and I guess the presumably related $2 billion increase short-term and long-term FHLB advances. Maybe a little more color on what the strategy is there. And then as a follow-up between the $2 billion in trading securities and then, of course, the $1 billion-plus jump in the warehouse, they really kind of dinged the TCE ratio. So just curious what your thinking is on the balance between strong regulatory ratios but a comparatively thin TCE ratio.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Let me address the $2 billion and the $1 billion, and then I'll let Jim chime in on the capital piece of it. So the $2 billion were securities that were kind of trapped in that period of time where there was Fed action going on, and we weren't able to get them off the balance sheet at the end of the month. We did deliver them into the hedges. Their hedge is in mid-April, I think, around April 15 -- 14, 15, so they're off the balance sheet now. So that's what that was. And then the warehouse, I mean, we've just seen the ability to increase our warehouse commitments grow as other warehouse providers haven't been in a position to take on more. And that's because we've kept a fairly low concentration limit on our warehouse business historically. And so given the fact that the opportunity is there in the market and then we narrow the collateral that we accepted on our warehouse lines. And then even reduce the advanced levels on certain collateral. So even though we're at a higher level in our warehouse balances, the risk associated with that, we feel very, very comfortable with. In fact, if you look at that page in the slide that's on our warehouse business, and I think it's 34, you can see the loss history there, and it's virtually nothing. So even if you go back into the financial crisis, it was $1 million a year there for 4 years. So we're really comfortable taking the level of warehouse exposure up given the spreads in that business and the low credit risk. So it does impact assets a little bit, but I think a trade-off is very, very helpful to us. So I'll let Jim then opine on the capital piece of that.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Yes. Thanks, Sandro. Just going back quickly, Scott. Just to remind you, at the end of the quarter, there was a lot of dumping of mortgage-backed securities going on, especially with like the Emirates because there were margin calls going on and those entities needed liquidity. That supply imbalance, I think, helped some of the dealers in that space get a lot more aggressive with their bids. And when we saw the bids for our Fannie, Freddie and Ginnie securities, and that's what comprises that trade securities line is newly created MBS that we weren't able to sell off our balance sheet at prices that we expected to get. We always had the option to deliver those securities into our TBAs and so rather than -- look, we didn't have to sacrifice execution at quarter end just to get those off the balance sheet. We had -- we let our capital levels go down a bit, and our balance sheet balloon a bit. We had the liquidity. We had the capital to be able to do that and deliver those into the TBAs mid month. So that's a big part of it. My remarks at the end, we continue to emphasize that when you look at Flagstar's balance sheet between warehouse loans, and Sandro elaborated on the credit loss content that we've seen historically there, and I think we've strengthened it even more so this past quarter, and loans held for sale. Between those 2 portfolios, I think you've got some pretty strong categories. Not to mention, 97% of our securities portfolio are Ginnie securities. So there's no credit risk implicitly in that portfolio. And then just look at some of the other categories we have on our balance sheet, you have roughly half our balance sheet. More than half our balance sheet is in categories that really have either no or very, very little credit risk -- credit loss content. So the 6.25% TCE ratio at the end, I think it's a little low. If you look at it on an average basis because as you're aware, warehouse spikes at the end of the month, at the end of the quarter. And also we had that end of the quarter back up on our trading securities. But as you're aware, if you look at -- those balances spike up at the end of the quarter, if you look at it on an average basis, the ratio is 7.25%, so 100 basis points higher.

Robert Scott Siefers - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Okay. Perfect. That's good color. I think, particularly on those $2 billion of securities because I think I had estimated that was just a loan, 60 basis points or so.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Yes. And just if I could, so all the things that you mentioned are kind of not related. So the looming of the balance sheet due to the backup of the trading securities on the balance sheet is different from what we're trying to do in terms of the long-term FHLB advances, which is, we think the rates are just attractive at these low levels. And given our rate position that I walked you through from a deposit and a loan perspective, we think it's the right thing to do now to lock in these low rates for that 3 to 7-year period of time.

Robert Scott Siefers - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Yes. No, I agree. I think it can be interesting, though. Just looking at the outside -- from the outside without that color, the almost a dollar-for-dollar match. So it looks like more of a conscious decision for some things that end up being sort of mutually exclusive. So that color is tremendously helpful. And I appreciate it.

And then separately, I was just hoping to ask on the gain on sale revenue. So I appreciate the color on the $90 million so far, and it certainly sounds like that transitory hedge stuff will not impact. So I can back into what sort of a core gain on sale margin would be. But just given all the fluidity in the mortgage market right now, maybe any sense for what sort of ongoing gain on sale margins might look like and the big factors impacting in your minds?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I'm not going there, Scott. I don't have the crystal ball. I can't tell you what the margins are going to be going forward. But what I said in my prepared remarks, I'll just reiterate and emphasize. If what Fannie thinks is going to happen, happens -- and by the way, it's not much different than what the NDA or Freddie thinks. I just picked Fannie for my prepared comments, if we have that kind of strength in the mortgage market going forward this year, then the opportunity to have gain on sale, maybe not at these levels, who knows. But they have continued gain on sale, strong gain on sale numbers, I think is -- likelihood of that is strong. And then similarly, that does great things for our warehouse business as well. And we did say it was over $90 million. It's actually now over $95 million. So this -- right now, it looks very good, but we're just not going to speculate on where it might go. And honestly, your guess is as good as mine.

Operator

Next, we'll move to Bose George with KBW.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

I wanted to ask about the loan subservicing business and how that gets impacted by the increase in delinquent loans, how you said the 9% loan requires more hands on approach. How does the contract work in terms of what you guys have compensated for that?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes. So Lee will obviously answer that one. That's the deal. But I'll just start by saying it's different when you're a subservicer versus a servicer, and I know that Lee will highlight that difference for you. So Lee, why don't you take this one?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO of Flagstar Bank*

Yes. Yes. Let me just pick up on the last point you made, and I made this in my prepared remarks. First of all, of all the loans we subservice or service, only 9% are owned by Flagstar. So that's a very small percentage. And from a liquidity point of view, it's going to be immaterial, just given our position as a bank and the available liquidity we have. In terms of our subservicing contracts, so there's a couple of things that are going on. As loans become more delinquent than the fees that we get do increase. But obviously, given the higher requests for forbearances and that activity, we've obviously had to increase capacity, first of all, on the collection side of the business. And we're now and have been increasing capacity in terms of loss mitigation activity because we know that is coming further down the line. So while there will be an increase in revenue the way the contracts are structured, there's also an increase in our cost base just given the higher activity levels.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

And Scott, no, I'm sorry. Bose, the other thing I would add is, if you look at our servicing portfolio, and they noted that it's under 10% of the total loans of service, it's not much different than your typical bank. So when you look at our servicing, our own servicing, it is very comparable to what any bank would have. It's the subservicing that's the big number. And as we articulated, that's a very different dynamic.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

And then can you guys also just give a little more detail on your credit positioning within the CLE exposures, particularly the hotel and retail and senior housing? Just sort of what do you think was the provision levels to go for those exposures in a stress scenario?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Yes. So I can't -- kind of like gain on sale, I can't tell you where the provision is going to go. I just know -- I just feel, like I said in my comments, that we're going to be looking at economics forecasts that are much, much different and worse at June 30 compared to March 31. But if you look at our portfolios -- so go to Page 31, and you see the commercial lending and then 32, the detail on commercial real estate and 33, the detail on C&I. I mean, especially look at 32 and 33, and look at each of those categories, and you just don't see any big number in any 1 category. And that's what we talk about relative to diversification as well as concentrations. The biggest number is in home builder at $900 million, and we haven't had 1 deferral request from our homebuilder clients thus far.

So when I look at this portfolio, and again, as I said in my comments, this is a $27 billion balance sheet that has less than $5 billion in commercial exposure. I don't think there's any other $27 billion bank in the country that can say that. And that's pretty low. So -- and then you look at the diversification that's here, and even in the syndicated portfolio, it's over 90-plus credits, that number comes from. And so the average balance on each is relatively manageable. And when you look at the loan-to-value ratios in our CRE portfolio, they're low. So I mean, if you really dig into the detail, we provided you a lot of detail on these pages. I think you'll see that the risk content is on the low end of the scale. And we're -- we've always been very conservative when it comes to our allowance, and we're not going to change that posture today. We feel very good about it based on the economic scenarios at the end of March, and we'll do the right thing by the allowance, come the end of June. But I don't have a crystal ball, man, to tell you what I think the provision could be in Q2. I just don't know.

Operator

And next, we'll move to Daniel Tamayo with Raymond James.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Just on the NIM and then how the PPP program impacts that. I think you'd mentioned that the NIM should be relatively flat in the second quarter, including the PPP benefit. How much benefit is assumed from PPP in that, if I heard that right, in that flatten in?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, I'll let Jim answer, but I don't think there's a real benefit from PPP to the NIM. Jim?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

That's correct. No, it's dilutive to the NIM that we would expect, Danny. But I would also say it's not going to be material.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

It's in the niche. Okay. I was assuming that there was some kind of recapture of fees in there, but if it's an immaterial number, then that's fine. All right. And then the floors in the warehouse business, did you benefit from those at all in the first quarter? And then how much would you -- how many -- or how much -- what percentage -- however much you could disclose are in the money at this point?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I don't know if I know the answer to the, how many are in the money per se. But we have bumped into to a lot of the floors. It's not that I don't want to give you that information. I just don't know that I know it off the top of my head. Jim does? Okay, Jim?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Danny, if you look at Slide 9, probably 1% of those warehouse loans have LIBOR floored at something higher than 0. So I think you can safely assume with LIBOR where it is today. And it just continues to come down to tighten the test spread on the difference between where LIBOR is 1-month LIBOR and Fed funds. So as that comes down, even more of those. But if you look at that 71% of that portfolio, have LIBOR something north of 0. A floor -- a LIBOR floor north of 0.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

And then just 1 last question. On the CRE portfolio, do you -- have you disclosed how much of that is construction?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Did we disclose how much of that is construction? Well, if you go to Page 32, and Jim, check me on this, but if you go to Page 32, you see the book value is $3.1 billion, the commitment level is 4.8. If we take the homebuilder piece out of it, the total commitment would be 3.9. So it would be something less than $800 million. And I don't know, Jim, if you know what that is.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

I don't have those answers specifically, Danny. But if you -- when you look at our December call reports and when you look at our soon to be filed March call reports, it will break out in the loan section, RCC, it'll break those amounts out for you.

Operator

And next, we'll move to Henry Coffey with Wedbush.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

So 3 questions. Number one, it's probably an editorial as well as a question. Given the reliance everyone has particularly on Moody's COVID forecast for their diesel adjustments, is there any risk that, that becomes countercyclical and starts affecting your lending decisions? I mean, obviously, your portfolio doesn't reflect the reserve add. It's all CECL related. And so we know that the Moody's forecast is more negative in April. It probably gets worse in May and June. And does that -- that could affect your reserving as you're stuck with the models, but does it affect your lending behavior?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I don't think it directly affects our lending behavior. I mean, indirectly, if the economy is continuing to weaken, then that has an impact on our decisions in the commercial areas, whether it's business banking, C&I or CRE. I mean right now, I don't remember the last time I looked at a commercial loan for approval. And we've tightened our approval process down such that 3 of us are Chief Commercial Officer or Chief Better Officer and myself have to sign off on every new commercial loan right now. And I -- like I said, I can't remember the last one I signed off on. As time goes on, as things get better, we'll make decisions to make commercial loans where we feel like a business has revenue confidence that allows us to have underwriting confidence. That's the problem right now. It's just very difficult to have confidence in cash flows with most businesses and so therefore, we've drawn back quite a bit. So I think our lending activities will probably be ahead of the Moody's analytics in terms of when we start lending, when more opportunities come about that makes sense, but I don't think there's a direct correlation.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

Great. And then 2 more questions. Obviously, a $90 million gain on sale revenue in 1 month is quite spectacular. Do you have enough insight into the pipeline to get a feeling for how May and June play out? Can you -- were there any -- are there any sort of aberrant outcomes in April that really changed that? Or are you just seeing a big flow of business and obviously, a return on gain on sale margins to where you would expect they would be, which is much higher?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Kristy, if I'm wrong on anything, correct me, but I don't think there's anything much different in April than March other than we didn't have the hedging challenges in April. The business continues to be very strong. The question, Henry, is can the margins continue at the levels they're at today? I think the volume for the next couple of months looks pretty good, but whether the margins continue, I don't know. And that was the question that was asked of me earlier that I punted on because I don't know. But I'll let Kristy add anything she'd like to that.

Kristy Williams Fercho - *Flagstar Bank, FSB - Executive VP & President of Mortgage*

Yes, Henry. I mean, one thing I'll share is, I mean, you only have to look at the strategy that we've really deployed over the last year, which is really evaluating those opportunities where we could optimize our returns through product, through volume and through channel mix. And then really just continue to focus on how do we bring value to our customers. And so we've continued that strategy in April as the market has really been dislocated over the last 2 months and really taking advantage of that to the $90 million plus benefit that we've seen. So there's no reason to expect that, that won't continue as we get into the future months, and our strategy will continue to be the same, optimizing that channel mix.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

So we can go back to looking at primary secondary spreads as kind of the guidepost as to what to expect. And given the volatility seen in March, that probably doesn't come up for a while. Is that a fair conclusion?

Kristy Williams Fercho - *Flagstar Bank, FSB - Executive VP & President of Mortgage*

Yes. And it's a great point that you bring that up because actually, if you look at primary, secondary spreads, these the historic high of 233 basis points at the end of March. And over the last 2 weeks, we've actually seen that tighten about 60 basis points. So that's a good measure of, obviously, the competitive dynamic in the market as well as capacity. And so you're absolutely right. I think that's a good thing to watch. We certainly watch that and pick in terms of what our pricing power is in the market every day.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

Great. And then moving on, on the servicing side. For you, it's not a question. You don't have to worry about service or advances. You've got plenty of liquidity. And as you pointed out on the call, owned MSRs are a small part of your servicing book. But maybe you could give us some insight into what's going on with your subservicing clients. Are they seeing an April of growing uptick in service or advance requirements? Are they -- are you working with them on this to provide a liquidity line to help them with this, given that the Fannie and Freddie are kind of sitting on their hands? I was wondering what your -- how does that business look like from the perspective of your clients? And what are you doing to work with them?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes. I'll let Lee give you the detail, but the only comment I'll make is, obviously, with 4 months maximum advance that the FHFA announced was, I think, a big relief to a lot of our partners. But yes, we're going to work with them, just like we're going to work with every commercial customer, and Lee can give you some detail on that.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO of Flagstar Bank*

Yes. I think you've hit the nail on the head, Sandro. I mean the FHFA announcement last week, it gave our subservice or MSR owners who we subservice for a lot of certainty because it effectively capped the amount of time that they would have to make the advances for. And so I think that was very helpful for all of them in being able to, from a liquidity need, plug it into their models and understand what they would want or what they may need. And then on the Ginnie Mae side, you've obviously got the PTAP program that Ginnie Mae has put in place. That's helpful. And of course, we work with partners where we can, and we do have some financing lines that are out there. And if we can be helpful in any way with our partners, we will do that. As I said, we're in the fortunate position that we're a bank, well capitalized. We have a lot of liquidity. And if it makes sense to do so, and we can help our partners, we will look to do that. But I think, I think the uncertainty that was there around liquidity maybe 3 weeks ago, 2 weeks ago, it's ease given the certainty that people now have with the FHFA announcement.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

I think you're in a great position. We've heard at least from the press that there's 1 or 2 major correspondent lenders that may walk away from that business. Do you have the capacity from a technology, and a people, and a lending perspective to pick up even more market share, if that's where we end up?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO of Flagstar Bank*

Yes. I mean, look, here's what I'd say. You never like to benefit from adversity or if others are struggling. I mentioned in my prepared remarks, we're servicing or subservicing a little over 1 million loans right now. And we have the capacity to service or subservice 2 million loans. And look, we will just continue to do what we've always done in terms of growing that portfolio. And we've been very successful in doing that up to now. And so as opportunities arise, we will evaluate them and see if they make sense. I'm certainly not going to talk about benefiting from others sort of falling down at this moment.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

Sandro, what did you want to say? I'm sorry, I cut you off.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes. I was just going to emphasize what Lee said. This isn't the time to look at significant growth in our servicing business. I think we take slow it and easy and take advantage of the really strong opportunities that may present themselves. But the way we've been building this business over time has been -- has worked really well, and we're just going to continue to file that same very thoughtful path.

Operator

And next, we'll move to Steve Moss with B. Riley.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Just 2 questions for me. You guys provided a lot of detail here, but just one on the non-interest deposit growth for the quarter. I apologize if I missed it. Just wondered if you could give some color there.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I'm sorry. You cut out on me. I couldn't hear your question. Hit me again, please.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Yes, sorry. On the non interest-bearing deposit growth for the quarter. Just wondering what the -- what were the drivers there? Any color there would be helpful.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes. I think it's primarily custodial deposits.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Okay. And then in terms of the disclosures around the leverage lending and the shared national credit portfolios here. Just wondering if you guys have any specific reserves for those portfolios. Any color there would be helpful.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, that's Page 37, where we give you that breakdown. And it is within the CECL model. Jim? (inaudible)

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

No specific reserves. 0 specific reserves on either of those portfolios. Okay. I'm sorry.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Okay. And there aren't specific reserves but -- let me just clarify, okay? There aren't specific reserves in the GAAP terminology. But when you look at the CECL model, each industry has reserves, obviously, which would all be part of both the leverage and the syndicated portfolio.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Okay. That's helpful. And then in terms of -- just wondering about the $35 million in loans that were special mention, are substandard at quarter end. Has that increased quarter-over-quarter? Or is that relatively -- just any dynamics there?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, it's relatively flat. Those had nothing to do -- yes, those had nothing to do with COVID.

Operator

And that will conclude today's question-and-answer session. At this time, I would like to turn the call back over to Sandro DiNello for any additional or closing remarks.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes. Thank you, Michelle. I'd like to close by talking about the Flagstar spirit. This company has come together in a way that I'll never forget, not just in the daunting deadlines, they have met and the crushing workloads they shoulder. But in the way they have brought fun into the things like the Flagstar COVID Facebook group, and a virtual happy hour, and company-wide photo contest showing their at home workstations. And while we've moved over 4,000 people to work at home, some folks do have to support bank branches, and some do have to be in an office building. And as you heard in Lee's comments, we are doing all that we can to put them in a safe environment and have rewarded them with over $1 million in bonuses. Plus, though we changed the work week for our branch employees to 4 days, we're paying them for 5, and we continue to pay employees who are not working due to the virus. We also set up an employee assistance program through our foundation to help employees experiencing COVID-19-related financial hardships. And in addition to the community support I noted earlier, we also opened our Paycheck Protection Program to nonprofits that were not previous Flagstar customers. Additionally, we set up a special small dollar loan program for people impacted by COVID-19 that live in low- to moderate-income areas. We know that we're in the fight of our lives, and we've given expressions of that sentiment with our "Flagstar versus COVID-19" T-shirts for every employee. We are tough, and we will prevail.

Finally, thank you to the entire Flagstar family, and I appreciate all you do more than my words can express and all of the best to everyone else listening. I urge to stay home as much as you can, and I pray that you stay safe and healthy.

Operator

And that will conclude today's call. We thank you for your participation.
