STRUCTURED FINANCE ASSOCIATION

Research Corner

July 28, 2020

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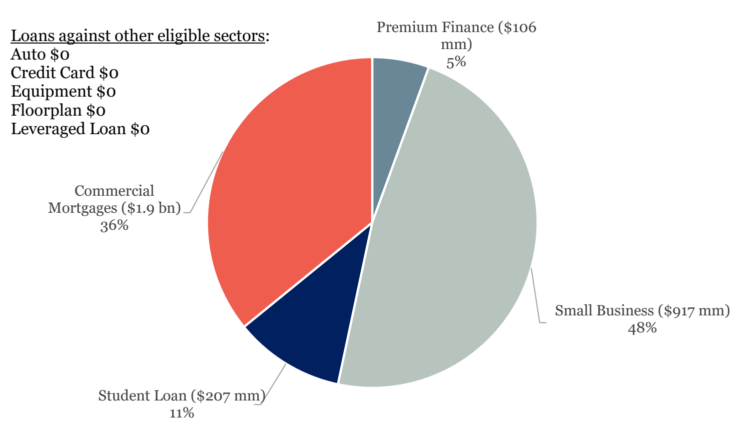
Research Corner - Market Signals

Market summary – The securitization market welcomed $7.5 billion of new bonds during the week of July 13, bringing July's total to $15 billion. Offerings consisted of $2.8 billion of non-agency RMBS, $1.5 billion of ABS and $2.42 billion of CLOs. CMBS contributed $400 million to the total. In the secondary market, the bid-ask spreads for triple-A rated bonds were, for the most part, unchanged to incrementally tighter for the week. Spreads in triple-A card and autos ABS have remained firm at June levels, while spreads on products that offered more yield such as ABS backed by subprime autos, private student loans, and personal installment loans, as well and CLOs, tightened by 3-5 bp as investors cautiously took on more risk amidst weaker macro indicators and rising virus cases. CMBS spreads, which gapped wider earlier in the month due in part to rising credit issues in the sector, tightened by 1bp over the week. The exception to these trends has been RMBS backed by jumbo loans which tightened by an impressive 21 bps as the mortgage market's V-shaped recovery continues apace.

By establishing the Term Asset-Backed Securities Loan Facility, or TALF, in March 22, the Fed signaled investors that it was safe to return the securitization waters, promoting additional lending to ABS issuers and returning much needed liquidity to the marketplace. An open securitization market allowed American consumers and businesses to continue to access credit affordably during this period of financial hardship. Without TALF, and the unprecedented level of fiscal and monetary support deployed by the Fed and the Treasury, it is unlikely that we would have seen such as rapid stabilization in the securitization markets.

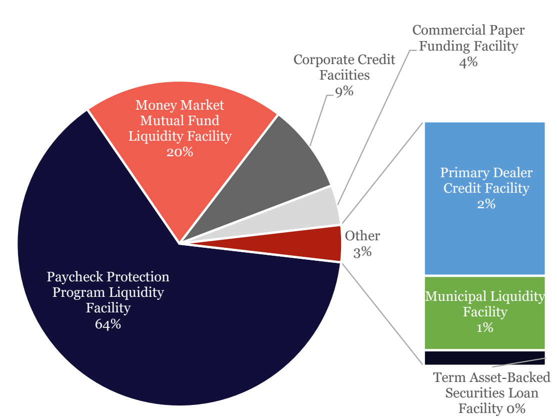
Spreads on most TALF-eligible ABS have tightened to the point that the cost of funding an ABS purchase through the TALF program may not be as economically attractive as funding without it. Current TALF usage supports this. As of July 21, the third subscription date, total TALF loan requests have reached $1.9 billion, with almost half of that going to fund the purchase of securitizations collateralized by loans made under the U.S. Small Business Administration's 7(a) and 504 loan programs, which may include PPP loans. Loans for the purchase of CMBS, premium finance ABS (which are backed by loans to finance property and casualty insurance) and private student loan ABS comprise the remainder. Absent from this list are loans to purchase ABS backed by autos, credit cards, equipment loans and dealer floorplan loans as these sectors have recovered significantly. We do not expect TALF usage by these sectors to grow meaningfully from today's levels, unless the broader securitization market retrenches, which, while unlikely, may occur if economic activity comes to a stop once again. As of June month-end, loans under TALF contributed less than 1% of the loans disbursed under the Fed's Section 13(3) lending facilities.

Total TALF loan requests reaches $1.9 billion, primarily for purchases of Small Business Loan ABS and CMBS



Source: Federal Reserve Bank of New York

Section 13(3) Lending Facilities – $107 billion total outstanding as of June 30. PPLF comprises 60% of total; TALF less than 1%

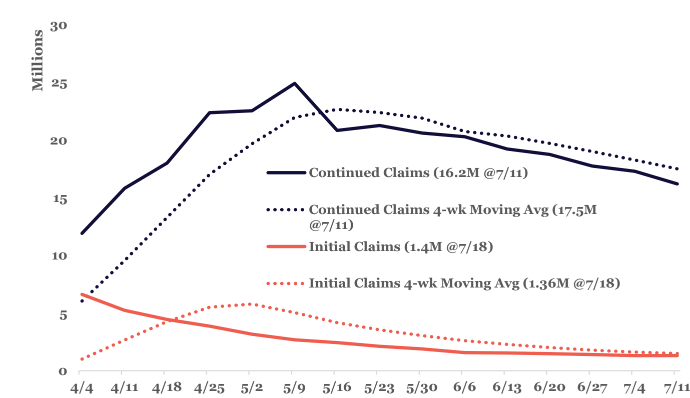


Source: Federal Reserve

What We're Watching

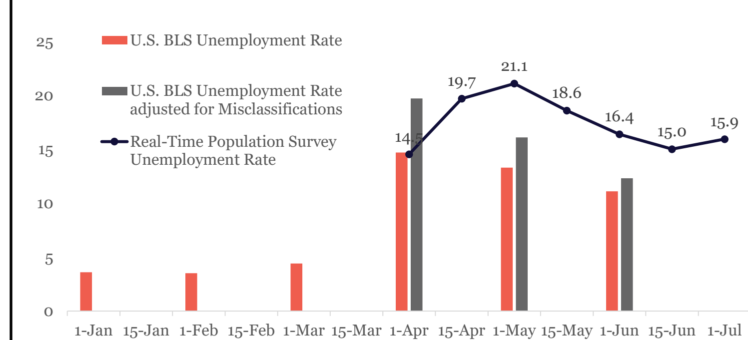
After falling for 15 consecutive weeks, initial jobless claims rose by 109,000 to 1.4 million for the week of July 18, two weeks before the Federal Unemployment Compensation Program, which added an additional $600 a week to an unemployed worker's weekly benefits, is scheduled to end. The weekly initial jobless claim data has been regarded as a metric that reveals timelier information than the unemployment rate about the effects that the fast-moving pandemic has had on the labor market. Recently, the Dallas Fed has offered the Real-time Population Survey (RPS) as an alternative to the official unemployment rate presented by the Bureau of Labor Statistics (BLS). The RPS generates real-time labor market statistics that are consistent with the official measures but are available up to six weeks earlier and updated twice as often. So far, the RPS has not shown the misclassification errors that has plagued the official unemployment rate. For the week of July 12-18, the RPS unemployment rate was 15.9%, an increase of 6% from the week of June 28-July 4. This is meaningfully higher than the BLS's unemployment rate of 11.1%, or 12.2% when adjusted for misclassifications, reported in early July for June. It is important to note that the BLS unemployment rate references the calendar week that contains the 12th day of the month. This is noteworthy as businesses have had to quickly adjust to various stages of reopening in response to rising virus cases. The proliferation of high-frequency data sources, such as RPS, seeks to address the information gap found in more traditional data sources.

Initial jobless rise 109k to 1.4M (as of 7/18); Continued Claims at 17.5M (as of 7/11)



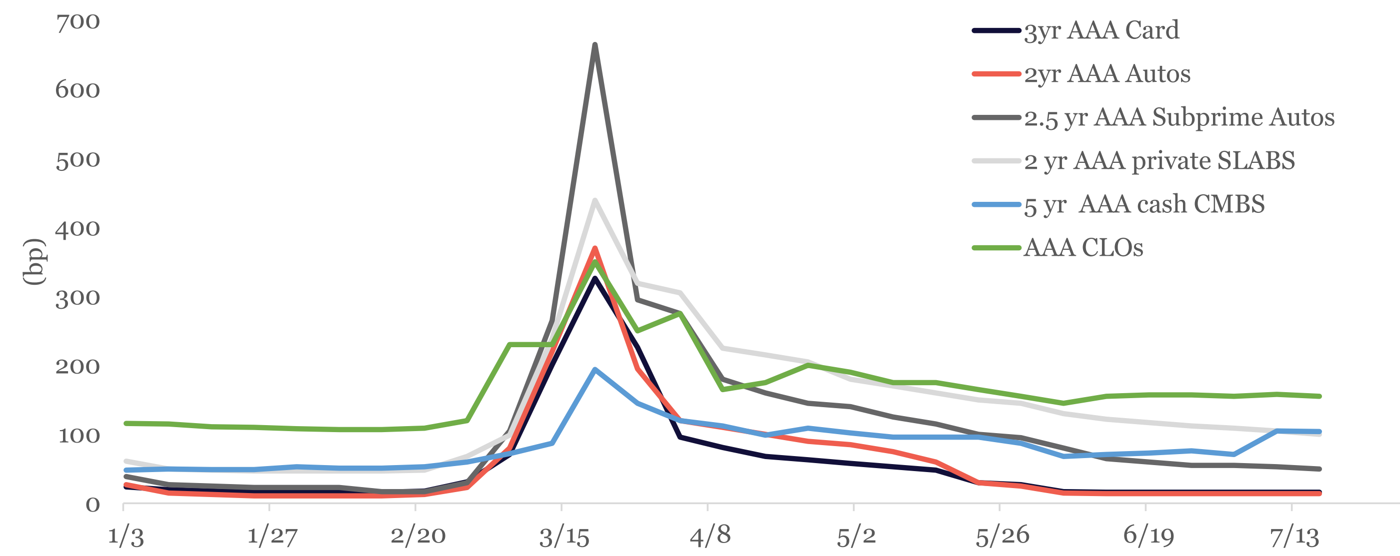
Source: Department of Labor

Dallas Fed's Real-Time Population Survey (RPS) shows unemployment rate at 15.9% vs BLS's 11.1%

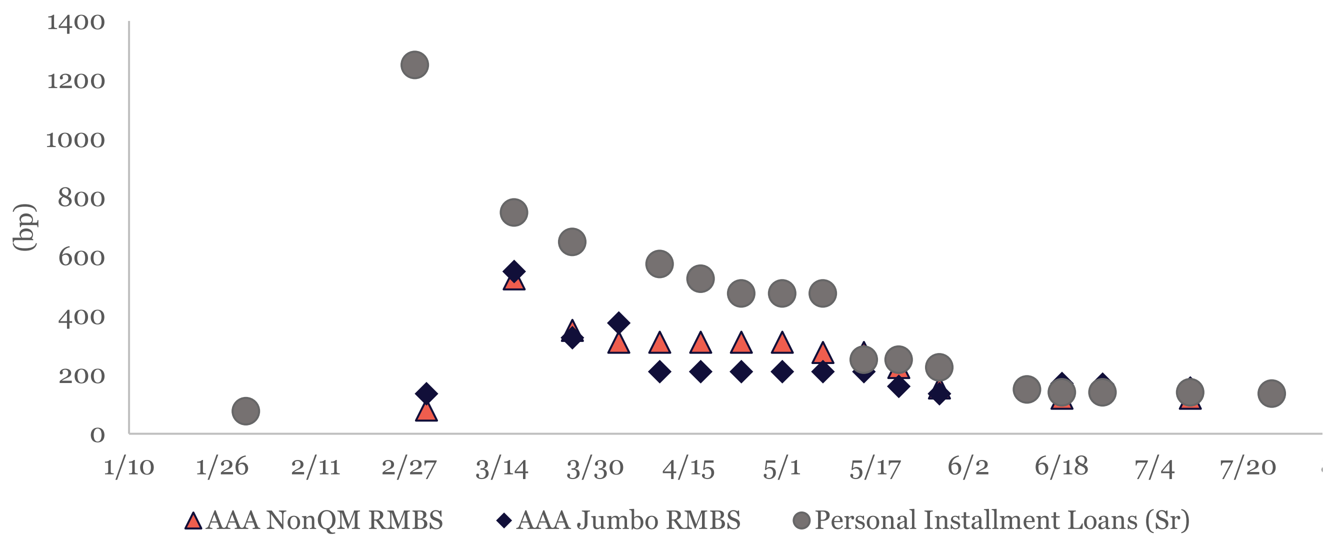


Source: Federal Reserve Bank of Dallas

Secondary Market Spreads

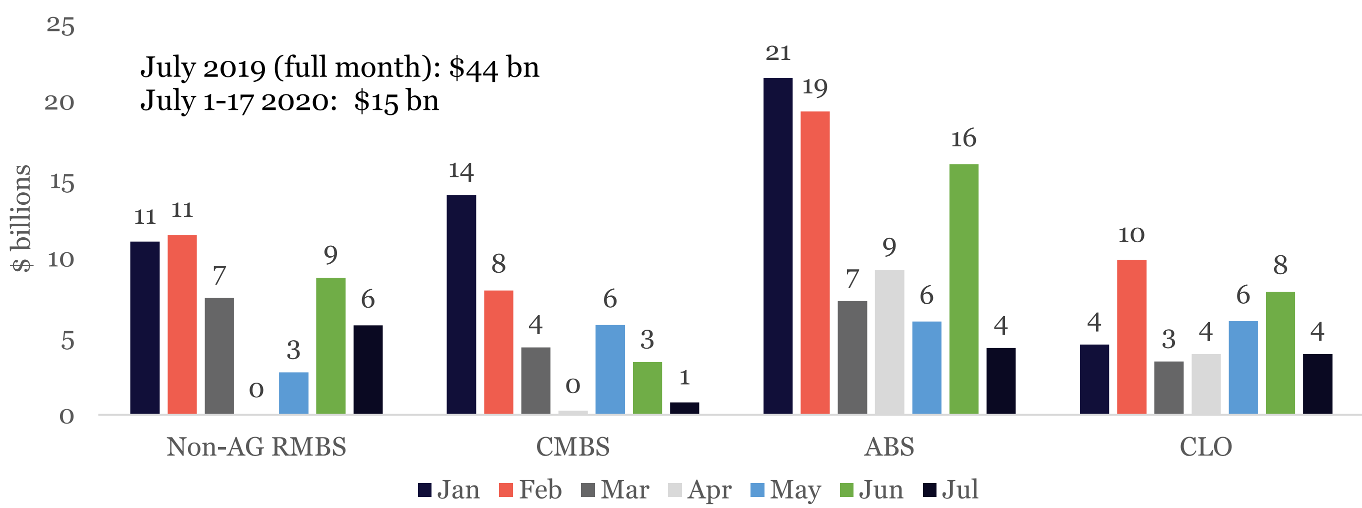


Source: Deutsche Bank Research



Source: Market Compilation

New Issue Activity



Source: Deutsche Bank Research