

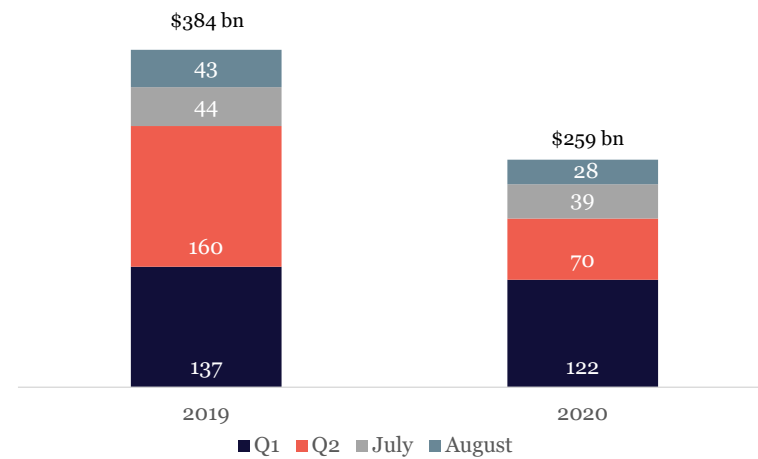
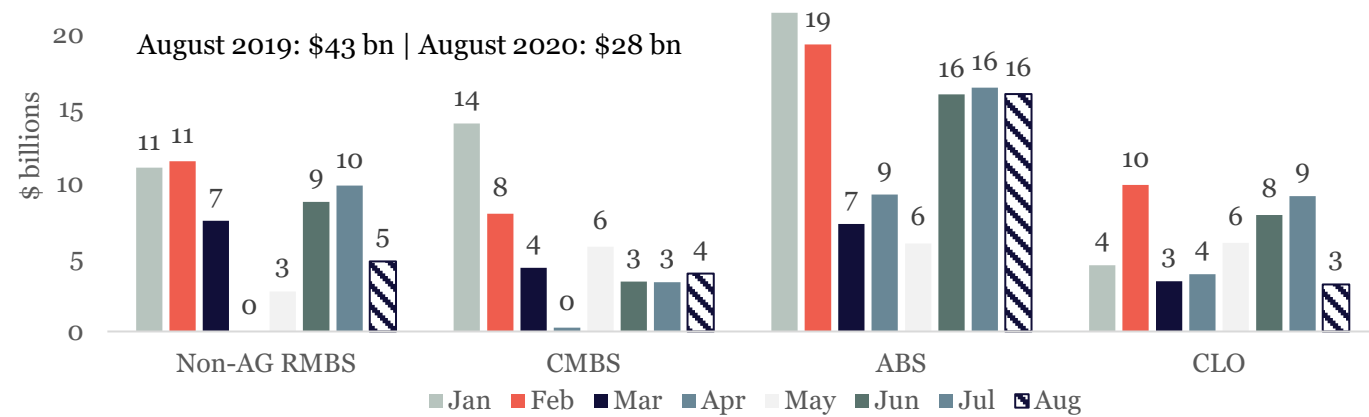


Research Corner
September 8, 2020

Research Corner - Market Signals

Market summary – Over \$28 billion of bonds backed by non-agency mortgages, commercial mortgages, consumer loans and corporate leveraged loans were offered in August, trailing the August 2019 level by 35%. New issue supply for the year now stands at \$259 billion, one-third below where the market was at this time last year. As issuers return to the securitization market for their funding needs, most market participants expect a flurry of new deals for the remainder of the year, barring the unexpected. However, as there are only four months remaining in the year, it is highly unlikely that supply will reach 2019’s full-year level of \$604 billion. The shortage of new issue supply will continue to support bond prices in the secondary market as investors turn to this market for inventory.

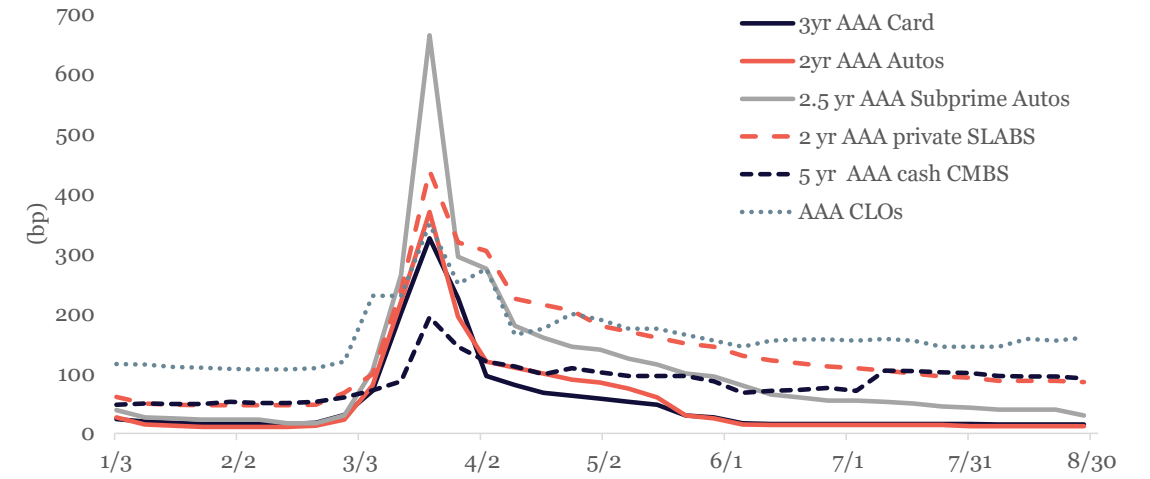
New Issue Activity



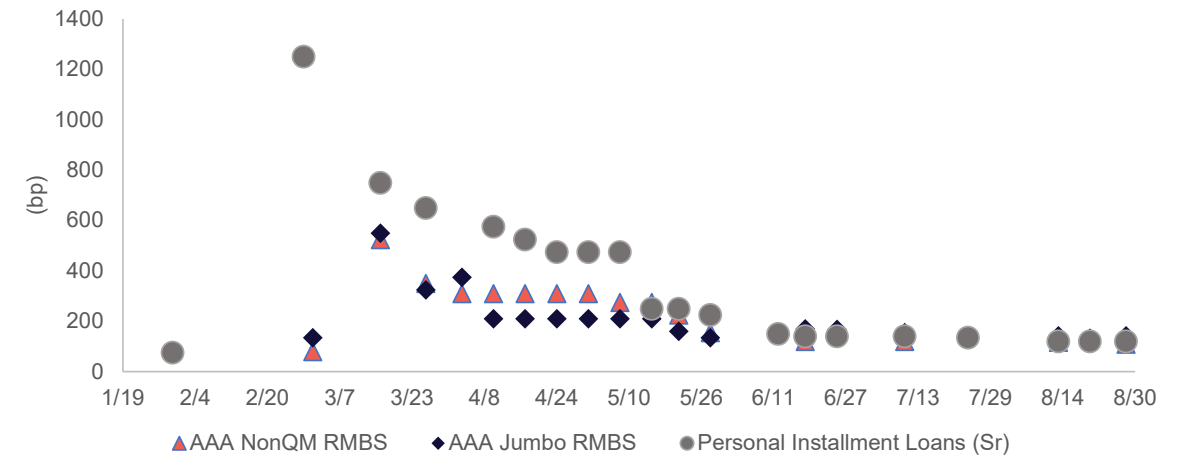
Source: Deutsche Bank Research

Strong demand for higher yielding products, such as ABS backed by subprime autos and non-QM RMBS, continued to push prices up, moving the bid-ask spreads for these products tighter in August. The spread for triple-A ABS backed by subprime auto loans tightened by 13 bp over the month to 30 bp, a seismic improvement from the 665 bp level reached in March. The bid-ask spread for non-QM RMBS tightened by 10 bp in August to end the month at 110 bp. While not quite back to pre-pandemic levels, today’s spread represents an 80% improvement over March levels. Demand for benchmark triple-A credit card and prime auto ABS remained robust, pushing prices for these lower-yielding but more liquid products slightly higher in August, moving the bid-ask spreads tighter by 1-2 bp.

Secondary Market Spreads



Source: Deutsche Bank Research

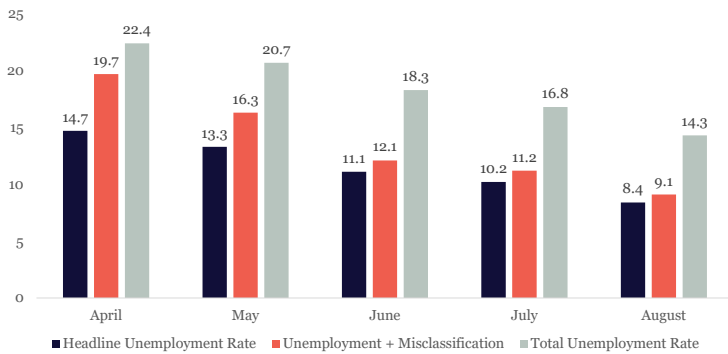


Source: Market Compilation

What We’re Watching

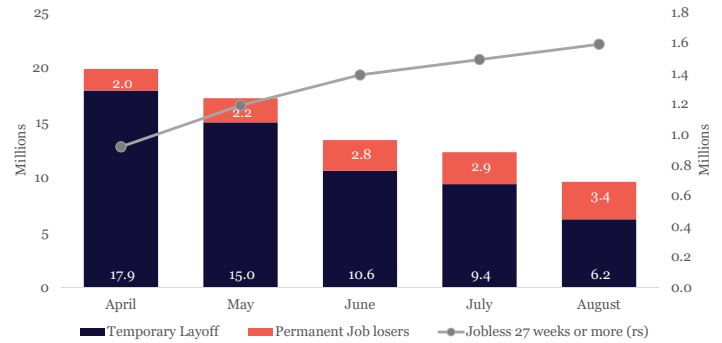
What we’re watching – The headline unemployment rate fell to 8.4% in August from 10.2% in July as 1.4 million jobs were added. This marks the fourth consecutive improvement for the metric, which is now 42% below the peak of 14.7% reached in April. Improvements in the headline rate, however, belie some troubling trends. While the number of temporary layoffs decreased by 3.1 million in the month, the number of permanent job losers increased by 534,000 to 3.4 million. This measure has increased by 75% from April. Also in August, the number of persons jobless for 27 weeks or more increased by 8%. The labor market may return some of these recent gains as some companies, across a wide variety of industries, have announced [layoffs](#) for fourth quarter, including MGM Resorts, Coca Cola, Salesforce, American Airlines and Boeing.

Unemployment rate improves for 4th consecutive month



Source: [U.S. Bureau of Labor Statistics](#)

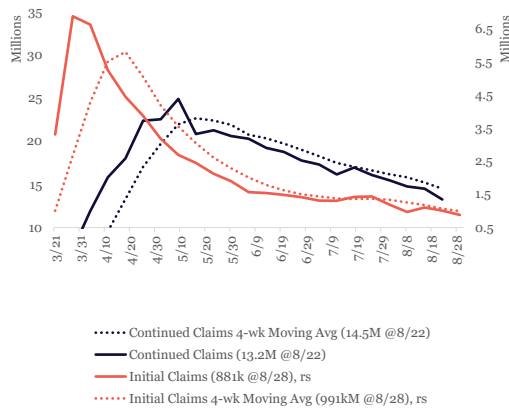
Temporary layoffs decrease by 3.1 million as permanent job losers increased by 534,000. Persons jobless for 27 weeks or more grows 8% to 1.6 million



Source: [U.S. Bureau of Labor Statistics](#)

The Department of Labor announced a change in the methodology used to smooth out the effects of seasonal factors on initial jobless claims data. The revision addresses the divergence between the adjusted and non-adjusted data as a result of coronavirus-related business closures. Using this methodology, the DOL reported that seasonally adjusted initial jobless claims for the week ending August 29 was 881,000. While this appears to be a decrease of 130,000 from the previous week's revised level, it's important to note that last week's adjusted level was calculated using the old methodology. For this week's data point, a look at the unadjusted metric may be more telling of the current situation. This data point increased by 0.9% to 833,352. Continued claims fell below 14 million for the first time since April, to 13.2 million.

Initial claims fall below 1mm for second time in August to 881k. Continued claims fall below 14mm for first time since April



Source: [Department of Labor](#)

Over 29 million individuals are claiming unemployment benefits; 51% are pandemic related



Source: [Department of Labor](#)

As with the unemployment rate, there is more going on under the surface as initial jobless data only captures claims filed under the states' traditional unemployment program. When including federal pandemic-related programs such as the Pandemic Unemployment Assistance and the Pandemic Emergency Unemployment Compensation, the total number of people claiming unemployment insurance benefits doubles. For the week ending August 15, over 29 million individuals claimed some sort of unemployment benefit. The August 15 number represents an increase of 2.2 million from the previous week and this is led solely by an increase in the Pandemic Unemployment Assistance program, which is scheduled to end on December 31.

Why is this important for the securitization market? Historically, there has been a strong correlation between the unemployment rate and delinquency and defaults on consumer loans. For example, during the 2008 financial crisis, mortgage delinquency rates rose by one point for every point rise in unemployment. So far, we haven't seen a rise in delinquencies or defaults as borrowers have benefited from supplemental unemployment benefits, stimulus checks and a myriad of deferrals and forbearance programs granted by lenders. As assistance expire and the labor market remains weak, loan performance is expected to track unemployment more closely- and this may come sooner rather than expected. President Trump's Executive Order on disaster assistance, which stepped in to fill the void left by the expiration of the \$600 weekly supplemental unemployment benefit mandated by the CARES Act, directs up to \$400 per week supplemental unemployment benefit to eligible claimants. Although the Executive Order will remain in place until a total of \$44 billions of federal funds are paid out or December 6, 2020, whichever comes first, the [Committee For a Responsible Federal Budget](#) estimates that there is just enough funding for five weeks.