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SFA Market Snapshot

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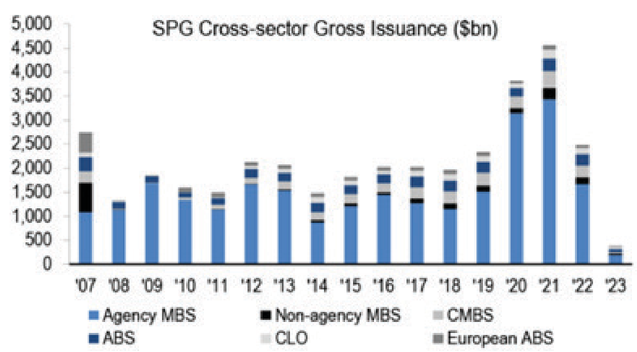
Issuance across the securitized space remains muted. As of April 28, 2023, issuance of agency RMBS reached $198 billion, tracking a 64% annual decline from 2022's level. Issuance across the private label sectors has been equally anemic. New supply of non-agency RMBS stood at $24 billion, CMBS at $32 billion, ABS $67 billion and CLOs $41 billion, according to J.P. Morgan Research. Credit risk spreads and trading volumes stabilized throughout the month as the securitization market incorporated banking turmoil news.

Cross-Sector Gross issuance ($BN)

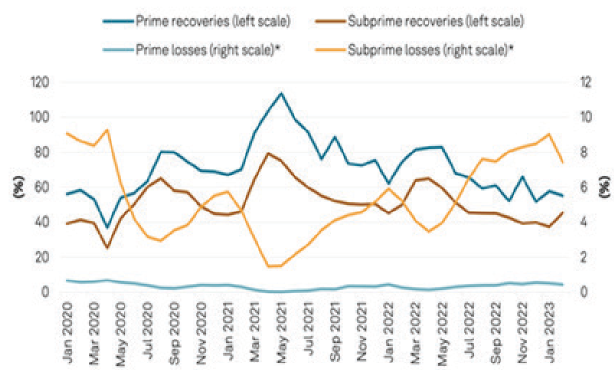


Source: J.P. Morgan Securitized Products Weekly, as of April 28, 2023.

Heard on the Street

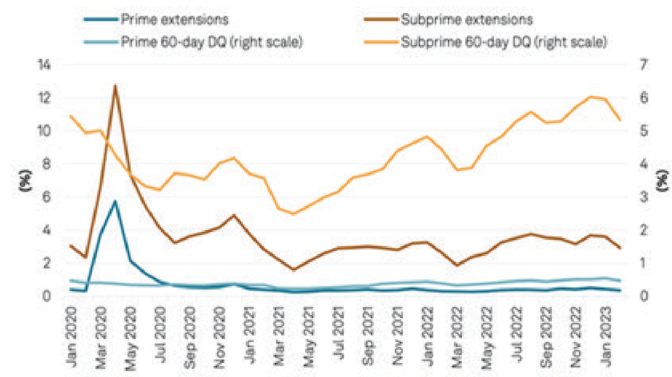
The ABS market is watching subprime auto performance closely. According to S&P Global Ratings, relief from tax refunds notwithstanding, delinquencies and losses in subprime auto loan ABS remain elevated. Losses ended February at 7.42%, after reaching a pre-pandemic level of 9.03% in January, the second highest reading since 2009. Similarly, 60-day delinquencies ended February at 5.33%, falling from January's record high of 5.96%. Performance has "deteriorated significantly" due to "multi-decade record inflation, loss of pandemic-related stimulus, and aggressive underwriting." The rating agency defines subprime auto ABS as transactions backed by loan pools with initial expected cumulative net loss rates of at least 7.50% (versus 3% for prime auto ABS), average FICO scores of less than 620 (versus 700 or higher for prime), and annual percentage rates that exceed 14.00% (versus up to 5% for prime).

Prime and Subprime Losses and Recoveries



Source: S&P Global Ratings, U.S. Structured Finance First-Quarter 2023 Chart

Prime and Subprime Delinquencies and Extensions



Source: S&P Global Ratings, U.S. Structured Finance First-Quarter

Despite higher losses, subprime ABS have, by and large, maintained their structural protections, helping this asset class weather credit challenges. Recent [Citi Research] shows that out of 280 outstanding subprime auto ABS deals, only seven deals (2.5%) have shown a reduction in overcollateralization, commonly referred to as OC, which is the difference between the principal value of bonds issued and the principal value of the underlying assets.

Auto ABS structures are robust and senior bond holders are well protected. These deals are typically structured with senior, junior and equity classes. Since principal is paid back sequentially, junior bond holders protect the senior classes from losses. In addition to OC, which is often set at predetermined levels and must be reached and maintained before junior bond holders are re-paid, auto ABS also benefits from excess spread and a non-declining reserve account. Excess spread represents the excess funds from the interest paid on the loans after trust expenses and is considered the first line of defense for bondholders. The non-declining reserve account is usually funded in cash at the onset of the transaction. These features have resulted in an overwhelmingly positive credit performance through the years, even in times of economic distress. To the extent that credit conditions worsen from here, we would expect auto ABS structures to, by and large, continue to exhibit that resiliency.