STRUCTURED FINANCE ASSOCIATION

SFA Research Corner

2024: Securitization's Surprisingly, Very Good Year

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2024: Securitization's Surprisingly, Very Good Year

As 2024 draws to a close, the securitization market has once again proven its resilience and adaptability. Against a backdrop of persistent challenges—including inflationary pressures, potential recessions, geopolitical tensions, and market volatility—the market delivered robust issuance volumes, strong investor demand, and the expansion of both established and emerging asset classes. These developments not only underscore securitization's importance in today's financial ecosystem but also set the stage for continued growth in 2025.

Robust Growth Across Sectors Amid Borrower Dichotomies

This growth occurred against the backdrop of mixed but stable consumer health, which continues to play a pivotal role in shaping securitization dynamics. While aggregate consumer health remains relatively strong, marked by low unemployment, elevated real household incomes, and increased net worth due to rising stock markets and home price appreciation, key challenges have emerged. Slower income growth, a lower savings rate, and rising delinquent payments on credit cards reflect caution among consumers and a shift toward slower consumption patterns.

Diverging Borrower Dynamics:

- Financial Resilience in Prime Borrowers:
  Rising disposable income and easing inflation benefited many households, stabilizing debt-to-income ratios even as debt balances increase. Prime borrowers, bolstered by financial resilience, continued to access credit markets confidently, supporting issuance in sectors like prime auto loans and prime jumbo mortgages.

- Strain on Near-Prime and Subprime Borrowers:
  In contrast, near-prime and subprime borrowers faced significant financial strain, grappling with higher-interest credit products and limited capacity to absorb economic shocks. Subprime delinquencies in auto loans and credit cards have risen, impacting related securitized assets and prompting cautious underwriting and investor reassessment in these sub-sectors.

Investors and issuers adjusted strategies to navigate the divide, targeting resilient segments while managing risks associated with more vulnerable borrowers. This adaptability contributed to the overall robustness of the securitization market, allowing it to thrive despite underlying challenges. Key areas of growth included:

- ABS: ABS issuance grew 19% to $304 billion, driven by gains in auto-related sectors, including a 30% gain in auto lease ABS. Concerns over credit quality have led to more selective lending, particularly for near prime and subprime borrowers, as noted in the Senior Loan Officer Opinion Survey (SLOOS). This cautious approach helps mitigate delinquency risks and will reshape the credit quality of securitized pools in 2025. The diversified "other" category jumped 54% to $64 billion, reflecting investors' continued appetite for non-traditional asset classes such as ABS backed by whole business securitizations, cellphone payments, data center securitizations and aircraft ABS.

- CLO: CLO new issuance surged 53% to $178 billion in 2024, driven by a 62% increase in Broadly Syndicated CLOs and a 26% rise in Middle Market CLOs. A resurgence in leveraged buyout (LBO) and merger and acquisition (M&A) activity fueled this growth, as the interest rate environment stabilized resulting in greater market certainty. Additionally, CLO refinancing and reset activity, which extends reinvestment periods and maturities for existing deals nearing amortization, soared to $255 billion—more than ten times 2023's full-year volume. In response to growing investor demand, CLO ETFs (Exchange-Traded Funds)—typically backed by a mix of higher-rated CLO tranches—surged to over $19 billion in assets under management, up from just $120 million in 2020.

- Non-Agency RMBS: Non-Agency RMBS issuance surged 81% to $143 billion in 2024, driven by strong activity in prime jumbo mortgages and single-family rentals. Home equity-related products, including RMBS backed by home equity loans, closed-end seconds, residential transition loans, and home equity investments, experienced a significant resurgence as homeowners increasingly tapped into their home equity. According to CoreLogic, total net home equity reached $17.6 trillion by Q2 2024, translating to an average of $315,000 per mortgage holder.

- Non-Agency CMBS: Issuance surged 120% to $101 billion in 2024, rebounding from 2023's meager levels. Growth was driven by strong activity in Single-Asset Single-Borrower (SASB) transactions, alongside some recovery in conduit and CRE CLO deals. Despite persistent negative headlines and weak performance in the office sector, the market began to transition from its downturn as stabilizing interest rates and elevated yields drew investor interest. Improved underwriting standards and structural enhancements further bolstered confidence, helping the market identify opportunities beyond its more vulnerable segments.

- Synthetic Risk Transfer (SRT): Synthetic transactions gained traction in 2024, with credit-linked notes (CLNs) contributing $1.6 billion to ABS issuance and over $5.5 billion since 2020. These structures, often referencing prime auto loans, allow institutions to manage capital and risk effectively, akin to reinsurance.

- Private Credit: Private bespoke credit (also known as private debt) solidified its role in 2024 as a complement to traded, bank-centric corporate lending. From filling financing gaps for middle-market companies that have limited access to the capital markets to providing bespoke, negotiated asset-based financing solutions, private credit has become integral to the financial system. With assets reaching $1.7 trillion in December 2023 and projected to grow to $3.5 trillion by 2028, private credit enhances market resilience by diversifying funding sources. Together, public securitizations and private credit form a symbiotic relationship that fosters liquidity, stability, and growth.

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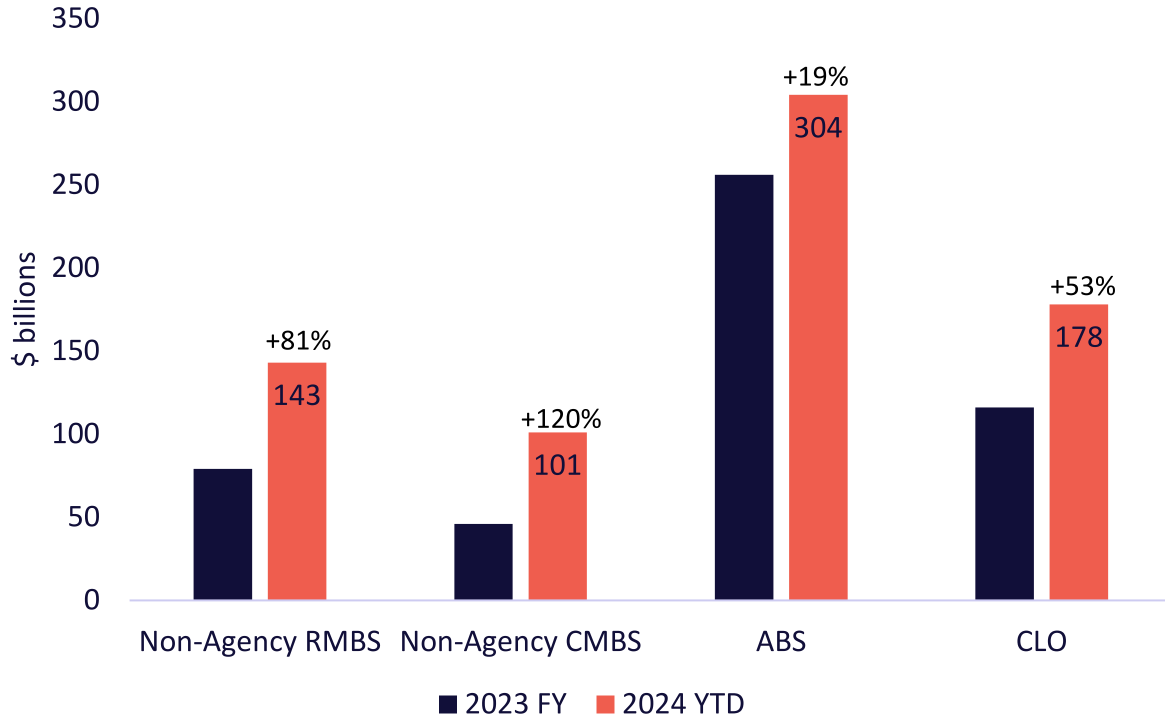
Excluding Agency: Robust Growth Across Securitization Asset Classes



Source: SFA Market Compliation

Diverging strategies among financial institutions also reshaped the market. Banks steadily reduced their exposure, with ABS holdings declining from $121 billion in December 2021 to $91 billion by mid-2024. Non-Agency RMBS and CMBS holdings fell to $52 billion and $61 billion, respectively. In contrast, insurance companies increased investments, driven by strong annuity demand and the search for reliable income streams. ABS/CLO holdings grew from $474 billion to $575 billion, and non-Agency RMBS holdings rose from $95 billion to $121 billion. These shifts highlight how institutional priorities, and regulatory considerations continue to influence securitization dynamics.

Evolving Investor Strategies ($ billions)

		Dec 2021	Dec 2022	Dec 2023	Jun 2024
Banks	ABS	121	111	99	91
	Non Ag RMBS	62	65	57	52
	CMBS	68	68	64	61
	CLO	156	171	166	156
Insurance	ABS/CLO	474	507	551	575
	Non Ag RMBS	95	104	115	121
	CMBS	290	285	277	273
Total		1266	1311	1329	1329

Source: Deutsche Bank Research

Looking Ahead: 2025 and Beyond

The securitization market's adaptability will play a crucial role in 2025 as it navigates a dynamic environment shaped by political, regulatory, and economic changes, many of which could present meaningful opportunities for growth and innovation. Political and regulatory shifts under President-elect Trump may play a big part in reshaping the landscape of housing finance, which makes up more than two-thirds of the securitization market. For instance, a potential delay in implementing the Basel 3 Endgame and housing finance reforms aimed at winding down GSE conservatorship could encourage banks to retain more loans on their balance sheets and boost issuance volumes in the non-Agency RMBS sector. Additionally, potential changes to education finance could pave the way for increased private sector involvement.

In addition to these policy shifts, the securitization market is expected to continue expanding into non-traditional asset classes, including a rebound in aircraft securitizations from post-COVID lows and growing activity in data center securitizations. In 2024, emerging categories like IP address lease securitizations and art loans gained traction, broadening the market's scope. Business models with predictable income streams and significant cash flow generation proved ideal candidates for securitization. As investors continue to search for yield in new asset classes, it is likely that more innovative categories will emerge in the securitization market. Additionally, advancements in Large Language Models (LLMs) and broader generative AI technologies are poised to improve transparency and efficiency in lending and securitization, further shaping market practices.

Consumer health and behavior will remain critical drivers of securitized asset performance. A focus on policies that reduce the cost of consumer credit and support economic growth will be essential to maintain market stability. However, disparities between higher-income and financially strained borrower segments will require careful navigation, emphasizing the importance of flexibility within securitized credit to adjust exposure and target resilient sectors.

As the market continues to evolve, its agility and focus on innovation will ensure its ongoing relevance. By addressing both opportunities and challenges, securitization will continue to be an important source of funding for consumers and businesses in 2025 and beyond.