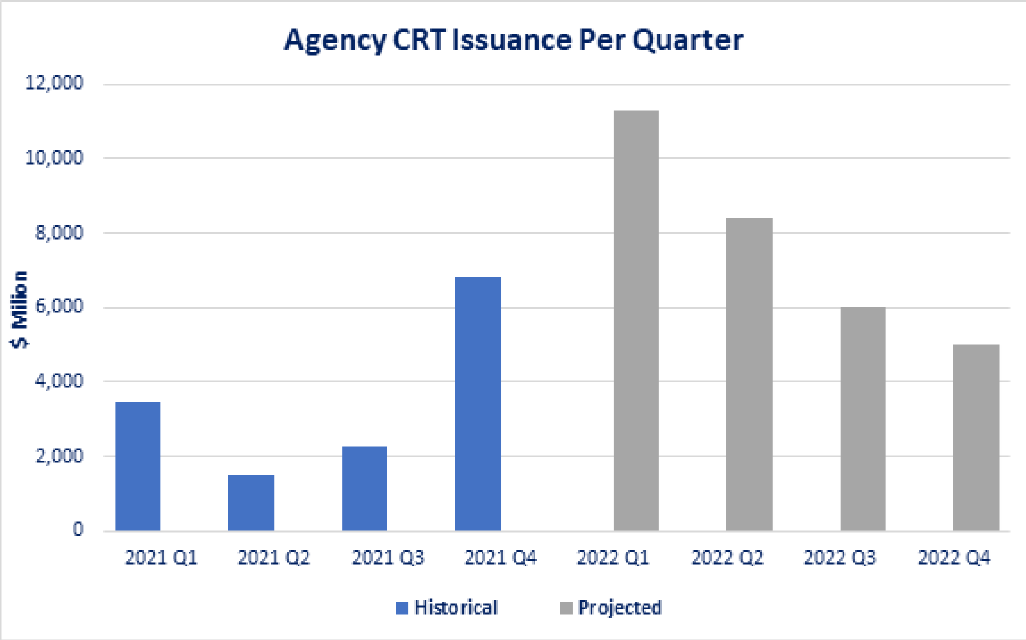
For Professional Advisers Only

Notes From The CIO

4 February 2022

- **We are entering a period of very attractive investment opportunities with outsized total return potential relative to the credit and cash flow expectations for many RMBS bonds**

- Technical pressures have continued to push Non-Agency RMBS spreads wider and prices lower. 2022's front end loaded supply wave continued this week with Fannie Mae's $1.2 billion CRT new issue. The deal took 2 days instead of 1 to complete because of tepid demand from buyers sitting on the sidelines, and resulted in spreads 10bps to 115bps wider across the capital stack. With a $2 billion Freddie Mac CRT scheduled to be priced next week, the CRT market and other RMBS sectors have seen significant technical weakness and could endure another week of softness



- Spreads on investment grade paper have widened by as much as 30-100bps, while mezzanine and subordinated bonds with strong credit quality have traded down in price by as much as 2 to 8+ points

- Today's structured products malaise is being exacerbated by broad bond market weakness from both rising rates and widening spreads given continued uncertainty surrounding the size and pace of the Fed's rate hikes and balance sheet reductions and implications to equity and corporate bond valuations, but we expect strong housing credit fundamentals to trump these macro concerns and highlight the strong value in RMBS. Most broad bond market indices are down more than 2% YTD

- Increasingly, the higher yields on all RMBS sectors and ratings categories is leading to extremely attractive investment opportunities characterized by low rate sensitivity, strong and improving credit fundamentals, and price appreciation opportunities. Adding to that, the floating rate characteristics of many of these bonds will lead to higher carry as the Fed raises rates

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- The supply technical will improve. RMBS new issue supply is already projected to slow, and as mortgage rates slow refinancing activity, origination will slow leading to fewer and smaller deals later in the year
- Our analysis shows continued build up of credit enhancement across RMBS profiles, as well as continued strength of homeowners, most of whom now have home equity of greater than 40% - a critical metric for continued loan performance
- These wider spreads and lower dollar prices represent an strong opportunity set as fundamental strength continues while technical pressures are forecasted to abate