For Professional Advisers Only

Notes From The CIO

29 July 2022

- RMBS prices and spreads continued to build support last week, especially in the more liquid Agency CRT sector and in higher rated profiles. We increasingly believe that we've seen the wides in this cycle, and we expect prices to continue firming, with this strength spreading from investment grade to below investment grade, from senior to subordinated profiles, and from more liquid to less liquid sectors

- Yields have more than doubled for most bonds, and have more than tripled for many shorter investment grade profiles – even as credit rating upgrades have accelerated and loan performance remains robust

- The Fed's 75 basis point hike last week will lead to sharply higher coupons for the third consecutive month on August 25th for floating rate profiles. Importantly, for Agency CRT bonds, which are floaters, the coupon is an obligation of either Fannie Mae or Freddie Mac, and rising coupons don't negatively impact credit enhancement as they can in Legacy bonds. We continue to focus on owning a significant allocation to floating rate mortgage securities

- Freddie Mac's STACR CRT new issue last week performed well. Each class finished several times oversubscribed even after Freddie significantly reduced yield spreads. The deal was smaller and Freddie retained the subordinated bonds – a reflection of lower supply to come, and recognition that spreads had moved to far. Next Monday, Fannie Mae is expected to launch their next CAS CRT new issue. This deal is also smaller compared to recent deals, and Fannie will retain the B2 subordinate class

- Non-Qualified Mortgage (Non QM) bonds have been the laggards recently, with the new supply pipeline slowing less than other RMBS sectors. We've begun seeing the weighted average coupon in the loan pools move up, improving the cash flow dynamics of these deals. We expect this to lead to better new issue execution, in turn supporting seasoned bonds' spreads. Many issuers have recently retained the subordinate classes in these transactions given the material widening in credit