Asset-Backed Securities and CLOs

Robust Issuance Expected in 2025

Despite tighter spreads, the outlook for structured credit remains attractive.

While the yield advantage of ABS over similarly rated corporate bonds has shrunk recently, we believe the sector continues to offer opportunities to earn excess yield. We expect 2025 commercial ABS supply to exceed that of 2024 due to tighter spreads, Fed rate cuts, and continued growth in capital-intensive digital infrastructure sectors. CLO issuance should remain robust in 2025 as demand from a range of buyer types has been strong.

Sector Commentary

- **ABS:** The ABS-corporate spread basis compressed after the presidential election, and it now ranks at its 58th percentile over the last ten years. In whole business securitization, sales figures reflect sustained labor and commodity inflation. Challenging fundamentals have weighed on equity valuations and invited private equity activity and associated ABS issuance.
- **CLOs:** Spreads have tightened across the capital stack as elevated repricing activity and limited new loan supply have pushed prices higher, making it challenging for managers to build par. Liability Management Transactions, or LMTs, continue to be a market focus, as recovery outcomes for the same loan could vary depending on the manager.

Investment Themes

- **ABS:** We favor senior exposures in longer duration commercial ABS backed by high quality collateral such as franchise royalties, fiber networks, and shipping containers. The new administration is expected to boost investments, further supporting consumers' excess savings. Still, uncertainty surrounding policies such as student loan repayment could strain individual borrowers. For this reason, we focus on subsectors such as home improvement loans, which offer exposure to high quality borrowers with structural downside protection via amortization and credit enhancement.
- **CLOs:** Both senior and mezzanine tranches are offering attractive value relative to similarly rated corporate debt. The basis between private credit (PC) and broadly syndicated loan CLO tranches remains historically tight despite elevated PC CLO issuance, but we expect this basis to normalize. Manager and credit selection are paramount, as attractive high level portfolio metrics may mask the true credit risk within these deals.

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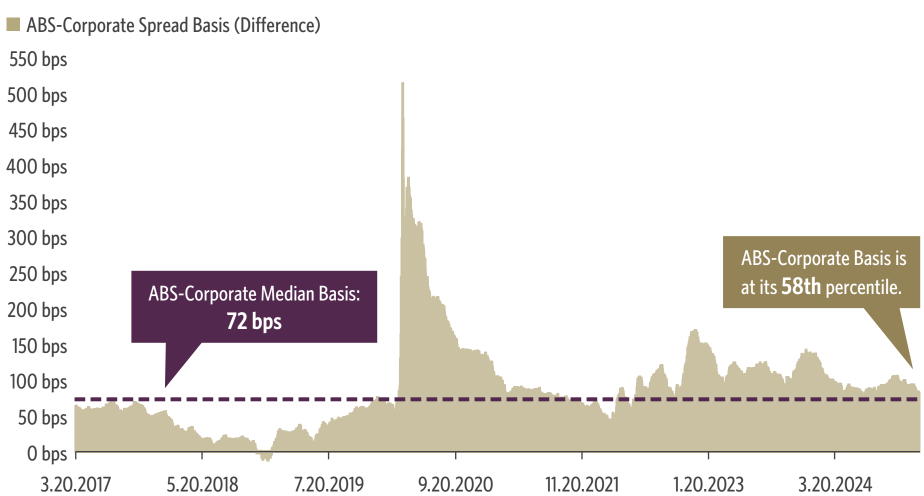
Commercial ABS Spreads Remain Attractive vs. Similarly Rated Corporates



Source: Guggenheim Investments, Bloomberg, ICE BofA. Data as of 12.31.2024.