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Non-Agency Residential Mortgage-Backed Securities

Constructive on Non-Agency RMBS

Low new-issue volume will limit supply and provide positive technical tailwinds for the sector.

The performance for non-Agency RMBS in the first quarter reflected broader market dynamics. Due to the macro volatility related to financial difficulties of regional banks, RMBS valuations experienced some softening to end the quarter. For instance, non-qualified mortgage (non-QM) AAA tightened by 40 basis points to start the year only to retrace all the tightening by the end of March. RMBS 1.0 and RMBS 2.0 subsectors—RMBS issued pre- or post-Global Financial Crisis (GFC)—posted 0.8 percent and 1.5 percent returns, respectively, in the first quarter, according to Citigroup data. Markets have trended with less volatility in the second quarter.

From a credit perspective, headwinds created by negative price moves in the housing market after June 2022 and an impending recession are meaningfully cushioned by conservative mortgage underwriting and more than a decade of underinvestment in housing relative to population growth in the United States. Additionally, tentative indications that home prices are near a bottom further reinforce the strength of the credit profile of RMBS. The latest CoreLogic reading for the month of February showed a 0.8 percent increase in home prices nationwide. It was the first positive reading since June of 2022. The price increase comes after several months of progressively smaller declines, which reached a peak of -1.1 percent in August of 2022. If the reversal continues, the improving housing market should modestly boost housing turnover-related prepayments which in turn provide an opportunity for capital appreciation for RMBS 1.0 and re-performing MBS deals that currently trade below par.

We remain constructive on RMBS credit, and the low new-issue volume will limit supply and may provide positive technical tailwinds for the sector. We see value in non-QM RMBS 2.0 mezzanine and senior tranches with investment-grade, typically stable weighted average life profiles, and RMBS 1.0 backed by loans with significant home equity. While typically carrying a low likelihood of principal loss, current investment-grade RMBS valuations reflect spreads wider than the long-run averages. These subsectors currently offer 5.5–6.5 percent yields and routinely trade at discount dollar prices.

By Karthik Narayanan and Roy Park

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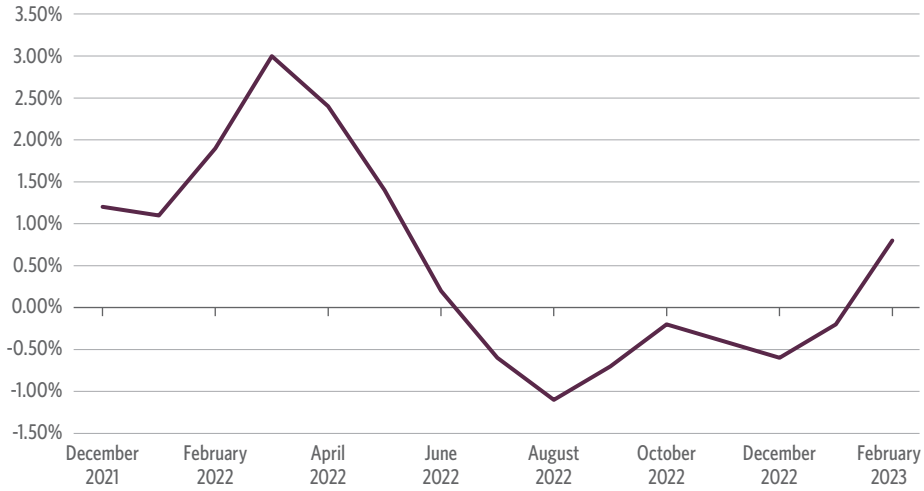
Home Price Growth Turned Positive After Months of Declines

CoreLogic Single-Family Price Change (MoM)



Source: Guggenheim Investments, J.P. Morgan, CoreLogic. Data as of February 2023.

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