

December 2023

Out-of-consensus calls for securitized products in 2024

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Santander US Capital Markets LLC

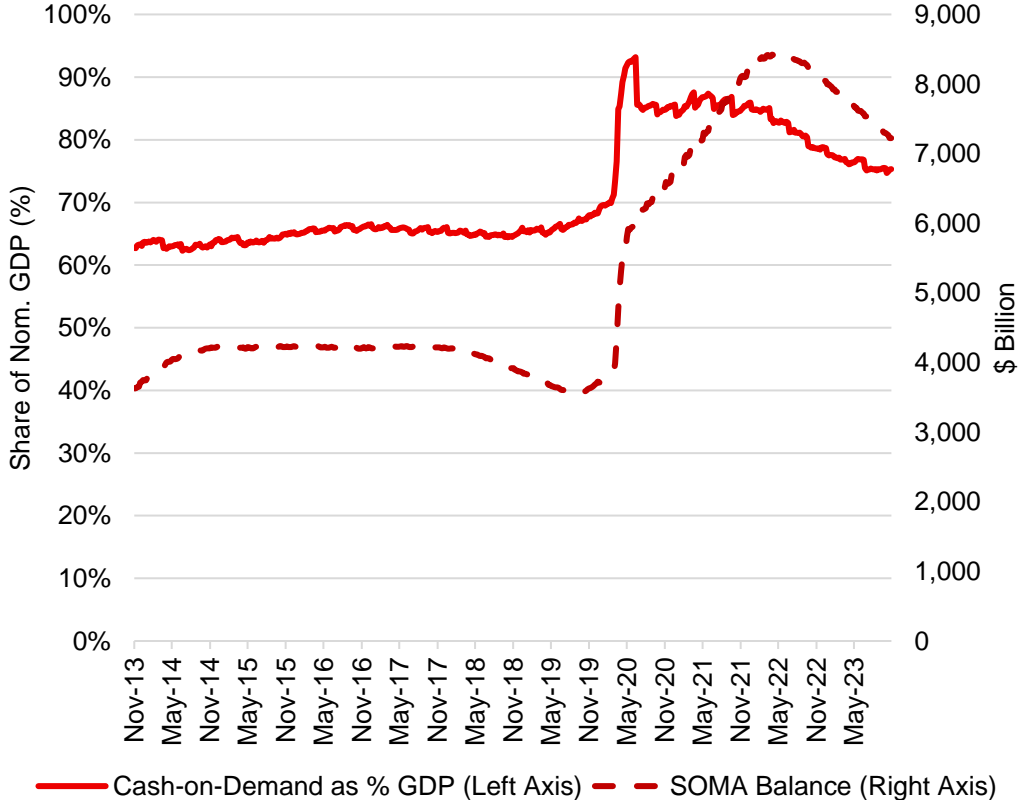
Economy: US economic outlook for 2024

Three out-of-consensus calls

- Economic growth may be slow, but momentum will dissipate gradually. Thus, first half growth should exceed second half growth.
- The Fed will not ease in the first half of the year
- Quantitative tightening will continue throughout 2024

Markets: Liquidity drops further

QT reduces available cash
 (Falling SOMA balances reduce cash-on-demand)



High short rates trap cash
 (Most MMMF balances go into riskless assets)

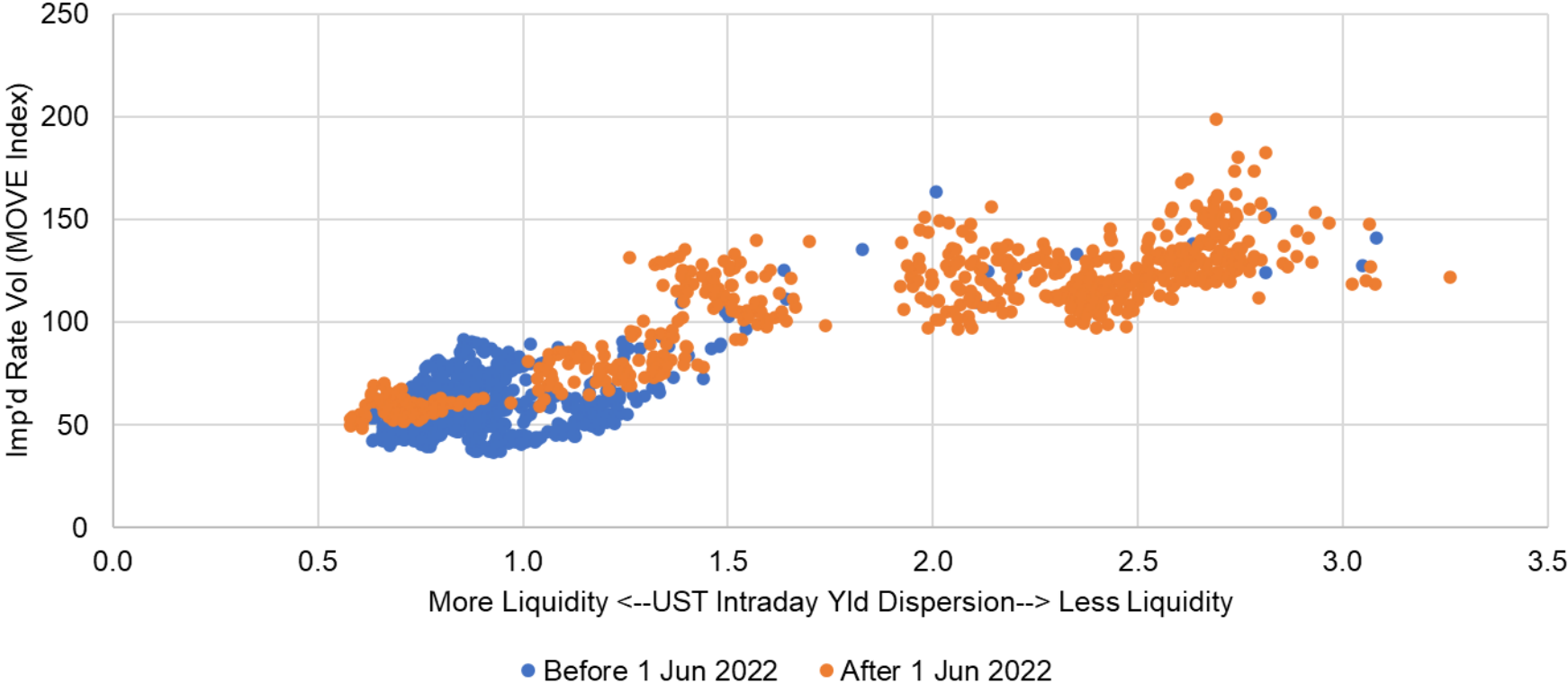


Source: Bloomberg, Santander US Capital Markets



Markets: Volatility stays high

Lower liquidity coincides with higher volatility
(Less cash available to police markets)

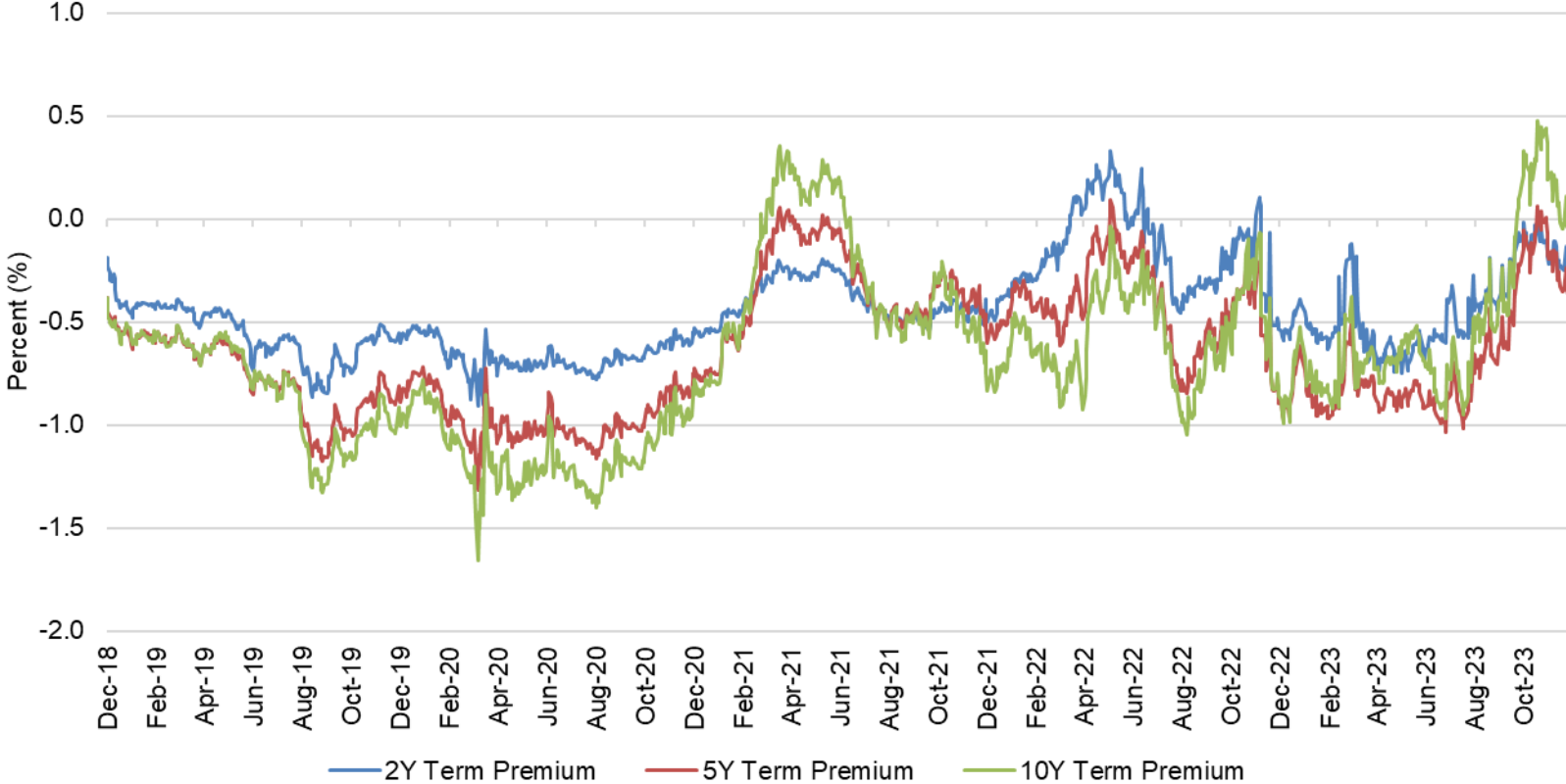


Source: Bloomberg, Santander US Capital Markets



Markets: Term and spread premium returns

Investors demand for compensation for volatility
(Term and spread premiums rise)

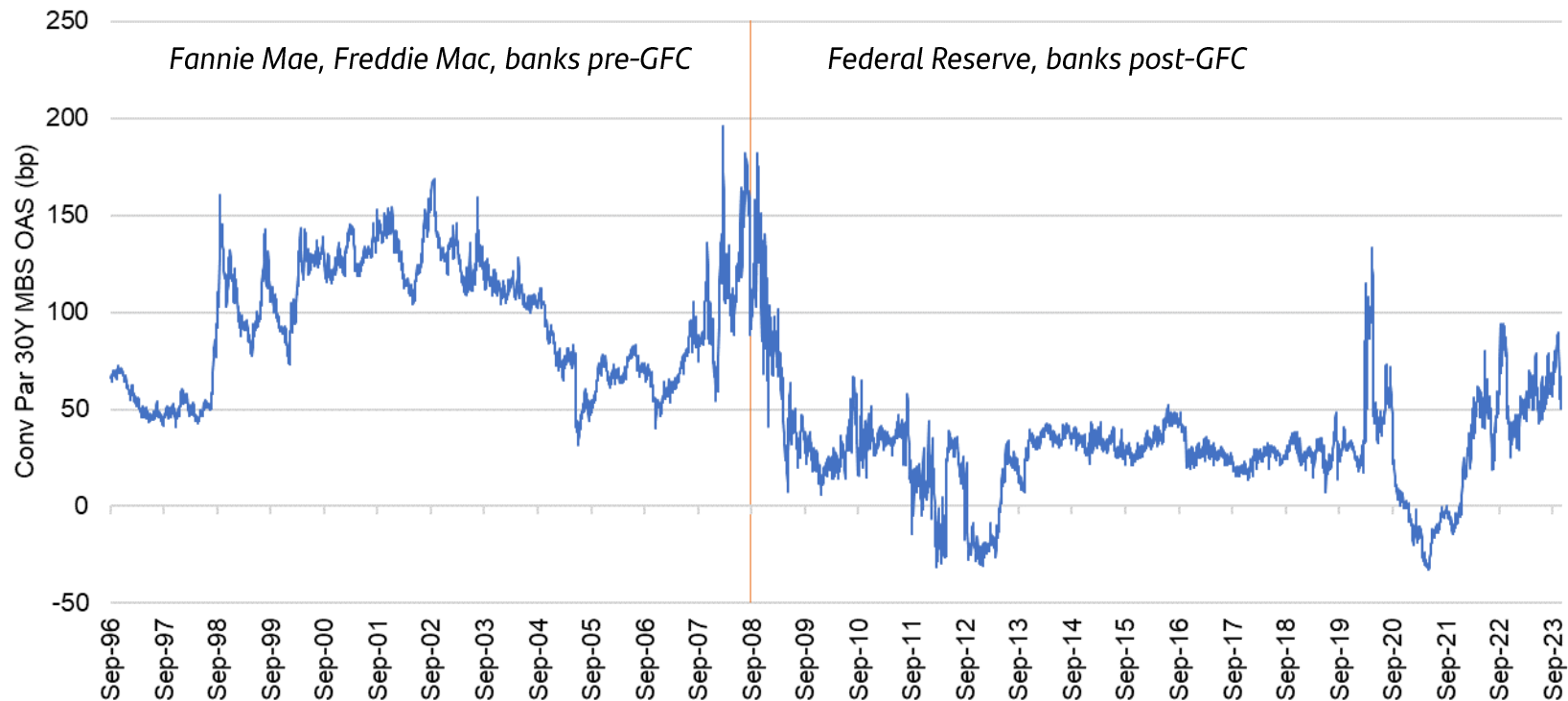


Source: Bloomberg, Santander US Capital Markets



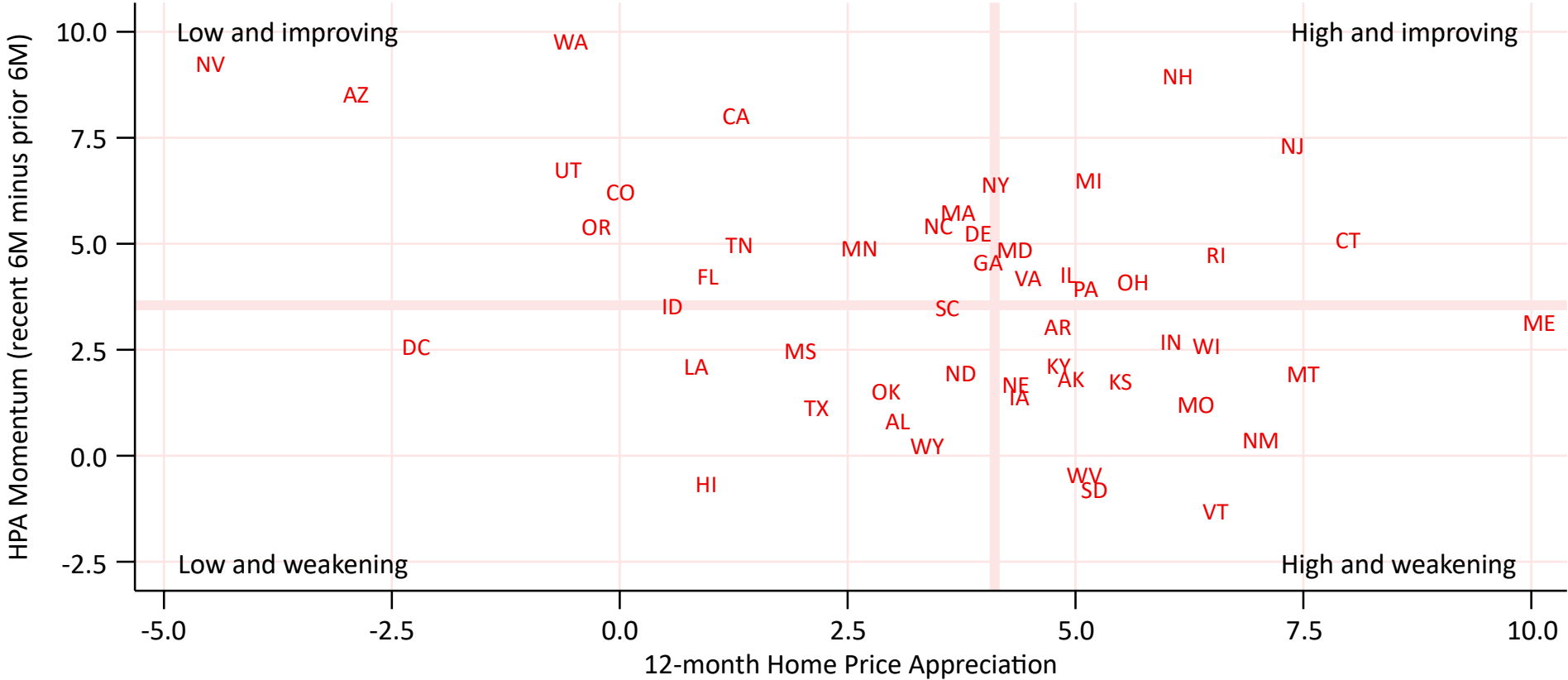
Markets: A pivot from policy to private portfolios

Marginal MBS pricing pivots from Fed, banks to TRR portfolios



Source: Bloomberg, Santander US Capital Markets

MBS: High HPA states lift turnover and returns



Source: Moody's Analytics, Santander US Capital Markets



MBS: Modest pickup in supply and turnover

Year	Gross Issuance (\$ bn)	Paydowns (\$ bn)	Net Issuance (\$ bn)
2015	1,259.8	1,092.5	167.4
2016	1,480.4	1,249.9	230.5
2017	1,314.4	999.1	315.3
2018	1,178.1	897.6	280.5
2019	1,538.9	1,316.4	222.5
2020	3,164.7	2,656.9	507.8
2021	3,486.2	2,616.7	869.4
2022	1,705.3	1,163.2	542.1
2023	1,022.1	765.4	256.6
2024	1,113.7	839.4	274.3

Source: eMBS, Santander US Capital Markets

MBS: Money managers primary source of demand

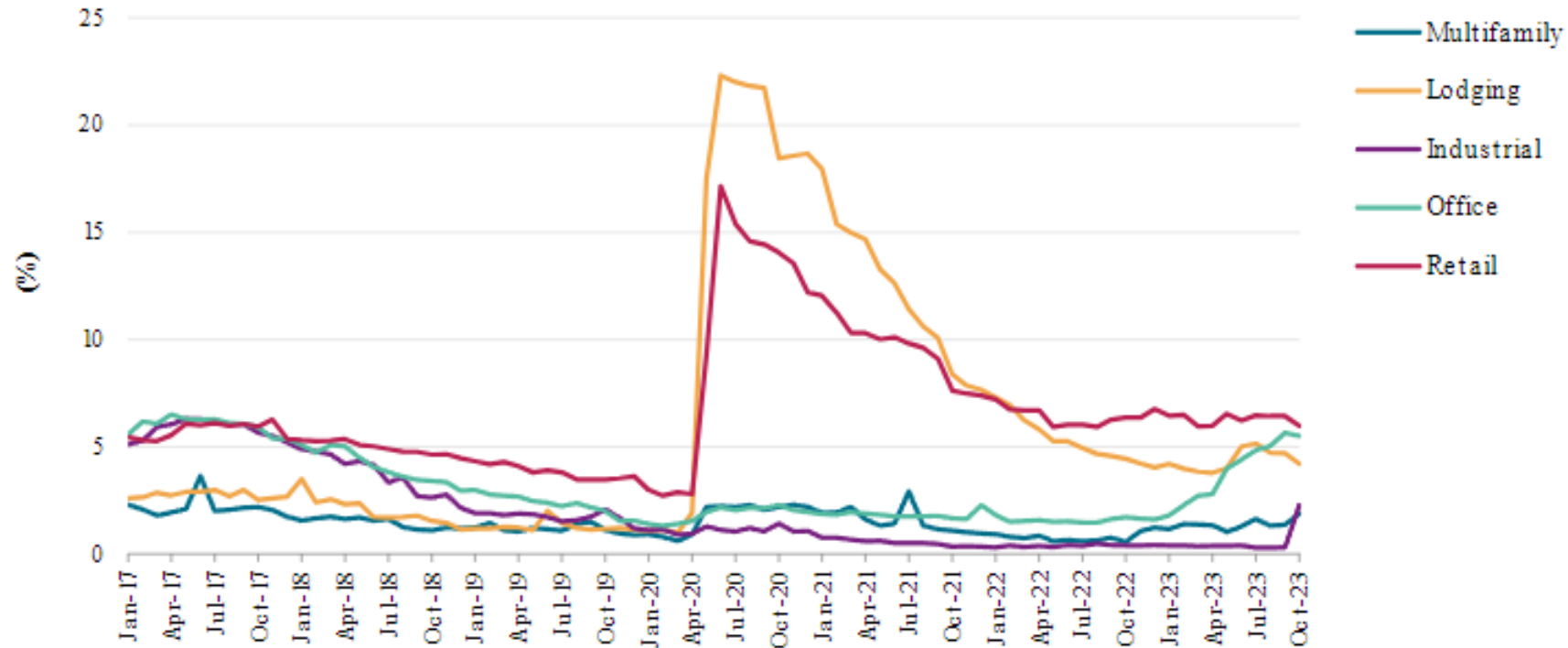
	Q4 2017	Q4 2018	Q4 2019	Q4 2020	Q4 2021	Q4 2022	Change since...		
							Q2 2023	Q4 2019	Q4 2022
Depositories	\$ 1,896	\$ 1,911	\$ 2,058	\$ 2,647	\$ 3,385	\$ 3,131	\$ 3,037	\$ 979	\$ (94)
Fed	\$ 1,765	\$ 1,644	\$ 1,409	\$ 2,066	\$ 2,606	\$ 2,633	\$ 2,530	\$ 1,121	\$ (103)
Foreign	\$ 909	\$ 970	\$ 1,100	\$ 1,105	\$ 1,188	\$ 1,239	\$ 1,316	\$ 215	\$ 77
Mutual+MMFs	\$ 715	\$ 860	\$ 926	\$ 750	\$ 352	\$ 590	\$ 798	\$ (128)	\$ 208
REITs	\$ 252	\$ 272	\$ 326	\$ 259	\$ 154	\$ 141	\$ 162	\$ (165)	\$ 21
St+Loc Govt	\$ 23	\$ 24	\$ 21	\$ 21	\$ 136	\$ 126	\$ 132	\$ 111	\$ 6
Pensions	\$ 187	\$ 220	\$ 266	\$ 208	\$ 132	\$ 188	\$ 197	\$ (69)	\$ 9
Life Ins	\$ 152	\$ 180	\$ 262	\$ 195	\$ 111	\$ 107	\$ 110	\$ (152)	\$ 3
GSEs	\$ 188	\$ 173	\$ 174	\$ 113	\$ 86	\$ 49	\$ 53	\$ (121)	\$ 4
P&C Ins	\$ 21	\$ 26	\$ 39	\$ 12	\$ 43	\$ 43	\$ 47	\$ 8	\$ 4
FHLBanks	\$ 127	\$ 135	\$ 142	\$ 38	\$ 26	\$ 30	\$ 30	\$ (111)	\$ 0
Brokers	\$ 38	\$ 58	\$ 78	\$ 77	\$ 15	\$ 109	\$ 107	\$ 29	\$ (2)
Unallocated	\$ 70	\$ 128	\$ 111	\$ 95	\$ 125	\$ 352	\$ 336	\$ 224	\$ (17)
Total: Fed+Dep.	\$ 3,661	\$ 3,555	\$ 3,466	\$ 4,714	\$ 5,991	\$ 5,764	\$ 5,566	\$ 2,100	\$ (197)
Total: All others	\$ 2,612	\$ 2,918	\$ 3,334	\$ 2,777	\$ 2,244	\$ 2,622	\$ 2,951	\$ (382)	\$ 329
Total	\$ 6,343	\$ 6,601	\$ 6,911	\$ 7,587	\$ 8,360	\$ 8,738	\$ 8,853	\$ 1,942	\$ 115

Source: Inside Mortgage Finance, Santander US Capital Markets

CMBS: A correction but not a rout

- Property prices should decline further, delinquency and default rates will rise, eroding borrower equity and credit support in deals.
- Lower volatility and lower interest rates should provide support for loans needing to refinance or for borrowers to sell properties, putting a floor under the market.
- Defense wins championships. To outperform, invest selectively in the more at risk sectors – floating rate agency loans and CRE CLOs.

Rising delinquency rates in CMBS are being driven primarily by office



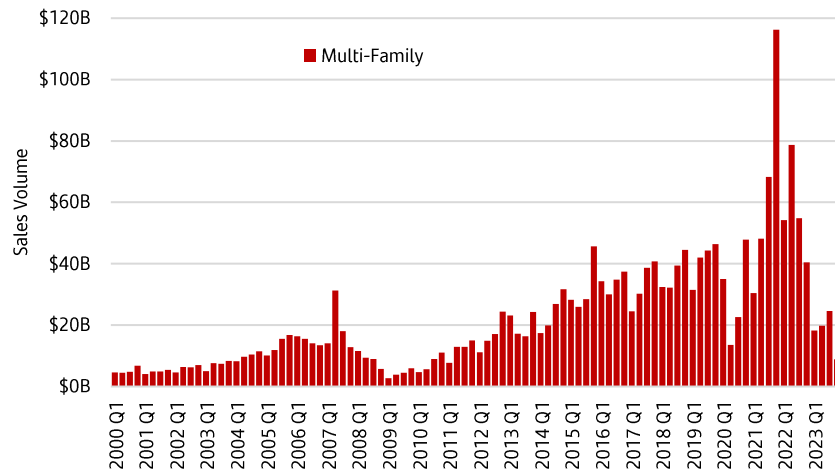
Source: S&P Global Ratings

- Delinquency and default rates for most property types will likely continue rising through at least the first half of 2024.



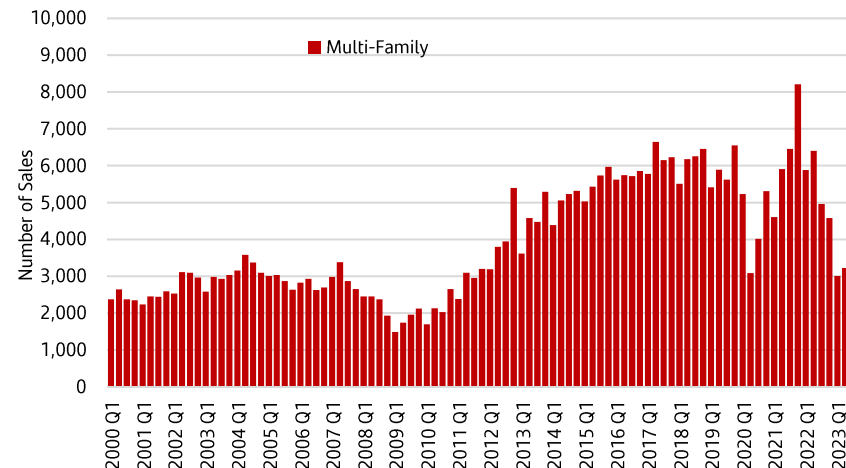
Multifamily market fundamentals have deteriorated sharply over the past year

Sales volume has averaged \$20 billion per quarter in 2023 (down 50%)



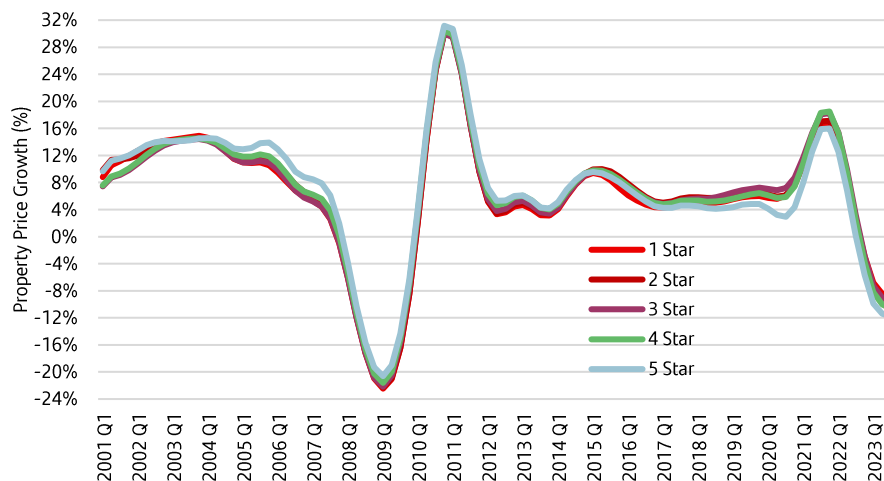
Source: CoStar, Santander US Capital Markets

That currently represents about 3,000 transactions per quarter (down 50%)



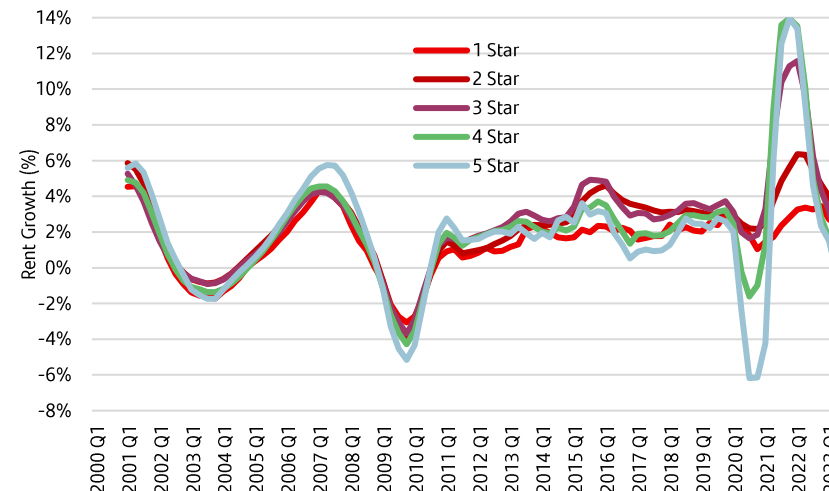
Source: CoStar, Santander US Capital Markets

Multifamily prices have declined by 8% to 12%, with 4 & 5 star down most



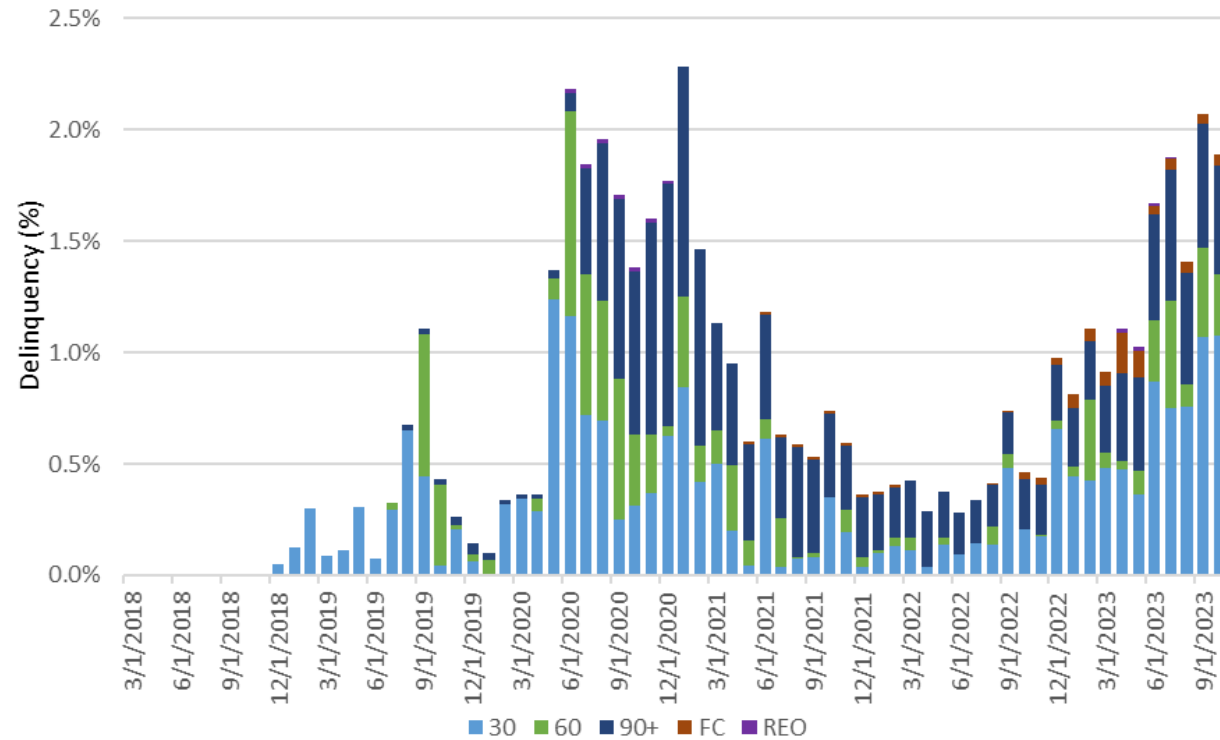
Source: CoStar, Santander US Capital Markets

Rent growth is now 0% to -2%, with high priced rents down the most



Source: CoStar, Santander US Capital Markets

CRE CLO delinquency rates have been also been rising



Source: Intex, Santander Capital Markets US

- Delinquency rates in CRE CLOs have risen to about 2.0% as of October 2023.
- These loans are transitional or bridge loans. All are floating rate, and most have interest rate caps. They are typically 3-year loans with two, 1-year extension options.
- Multifamily performance in CRE CLOs is somewhat better, but overall multifamily comprises 71% of collateral.



CLOs: Outlook 2024

- A small subset of BSL CLOs are most vulnerable to loan downgrades, whereas newer vintage CLOs may benefit from positive credit trends seen in this year's new loan issuance.
- Retail investors have become the fastest-growing investor group in CLOs. CLO ETFs may continue to expand, while demand from institutional investors remains vulnerable to regulatory headwinds.
- CLO issuance may stay resilient in 2024.

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