News Analysis

# Game-changing potential

**In the second in our series of year-end interviews with investment managers about where they expect to see value in 2022, SCI caught up with CRT market veteran Seer Capital**

Opportunities for investment in CRT trades from US names will increase significantly in 2022, says Terry Lanson, a portfolio manager at Seer Capital.

"We think we'll see significant volume out of the US and also out of Europe. The programme is growing in adoption globally. It is receiving significant attention from investors and capital allocators like state pension funds. More and more capital is being allocated to the space," he says.

Seer Capital, which manages approximately US$1bn in net assets, has been an active SRT investor since inception in 2008. Seer has grown SRT significantly in 2021 in a number of its accounts, including an SRT-focused separately managed account. This growth underlines the faith in the market and the rewards it offers.

Not only will the traditional names like JPMorgan and Citi hit the market in 2022, but also new names will, it is hoped, get involved. The addition of more tier one names would be a game-changer.

"If, say, Bank of America and Wells Fargo were to join the fray, then these two plus JPMorgan and Citi would be responsible for a huge amount of issuance relative to mid-size European banks. We definitely see the US market catching on to this product," adds Lanson.

JPMorgan has been a prolific issuer over the past year to 18 months, and especially so in the fourth quarter. Citi - the pioneer of the market in the US - has also had a very active second half of the year. These issuers are expected to come to the fore in 2022, though Q1 is traditionally not the busiest period.

Thus far, JPMorgan has favoured the auto loan market, with three CLNs issued referencing auto loans sold this year, but it is expected to spread its wings into the corporate loan space in 2022. The fundamental structure has been tested and proved successful.

Moreover, it continues to be bound by the strictures of the standardised approach to assessment of RWAs under the terms of the Collins Amendment, as are other tier one banks in the US.

"The largest banks are still constrained by the standardised approach, so it behoves them to issue CRT backed by relatively low risk assets because they get the same amount of relief," says Lanson.

Of course, Texas Capital Bank and Western Alliance Bancorporation broke the ice this year and became the first US regional banks to bring CRT deals, so the way is now opening for second and third tier US banks to issue in the sector. The structure is now seen to be robust, and has attained regulatory approval. The stars would seem to be aligned in 2022.

Both the Texas and WAL deals securitised mortgage warehouse loans, which are viewed by regulators as consumer loans and thus get the full 100% risk weighting under the standardised approach. However, they are not risky assets, and thus did not reward investors as handsomely as in Europe.

The Texas deal paid Libor plus 450bp and the WAL trade paid Libor plus 550bp. This would not normally be a wide enough coupon for Seer Capital. Lanson looks for a coupon in the high single digits, which with the added spice of a pinch of leverage, will generate something in the region of Libor plus 13% or 14%.

"To get plus 550bp to 13%, you need a lot of leverage," he notes.

However, if the tier one banks like JPMorgan and Citi were to create collateral pools of, say, corporate loans, leveraged loans, or SME loans, then the coupon is more likely to be enticing. Citi has, it seems, looked at creating collateral pools from capital call facilities as used in the private equity market and this too would produce coupons that should make traditional CRT buyers sit up and take notice.

It should be noted that these assets are still viewed as low risk and will be priced relatively tightly, but just not as virtually risk-free as warehouse loans. Texas Bank, for example, has never experienced a default in this market. Its deal is said to have been bought by real money accounts.

There has been significant volume from the CRT market in 4Q21, leading to fears of over-supply and price erosion. However, it seems that more new investors came forward to meet the new supply and by the end of Q4 pricing was much in line with where it was at the beginning of October. A couple of issuers did try to push the market, but in the end priced deals at levels not originally under discussion.

Lanson, in short, is full of optimism for the market in the US. “The regulatory regime is now set and understood. The more it is tested and the less uncertainty there is, the better. We saw a very healthy market in Q4 and that is what we believe we will see going forward,” he predicts.

Simon Boughey