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Reg Cap Recap

A biweekly update on the Regulatory Capital Relief/Significant Risk Transfer sector

July 15, 2025

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Reg Cap Fundamental Credit Trends

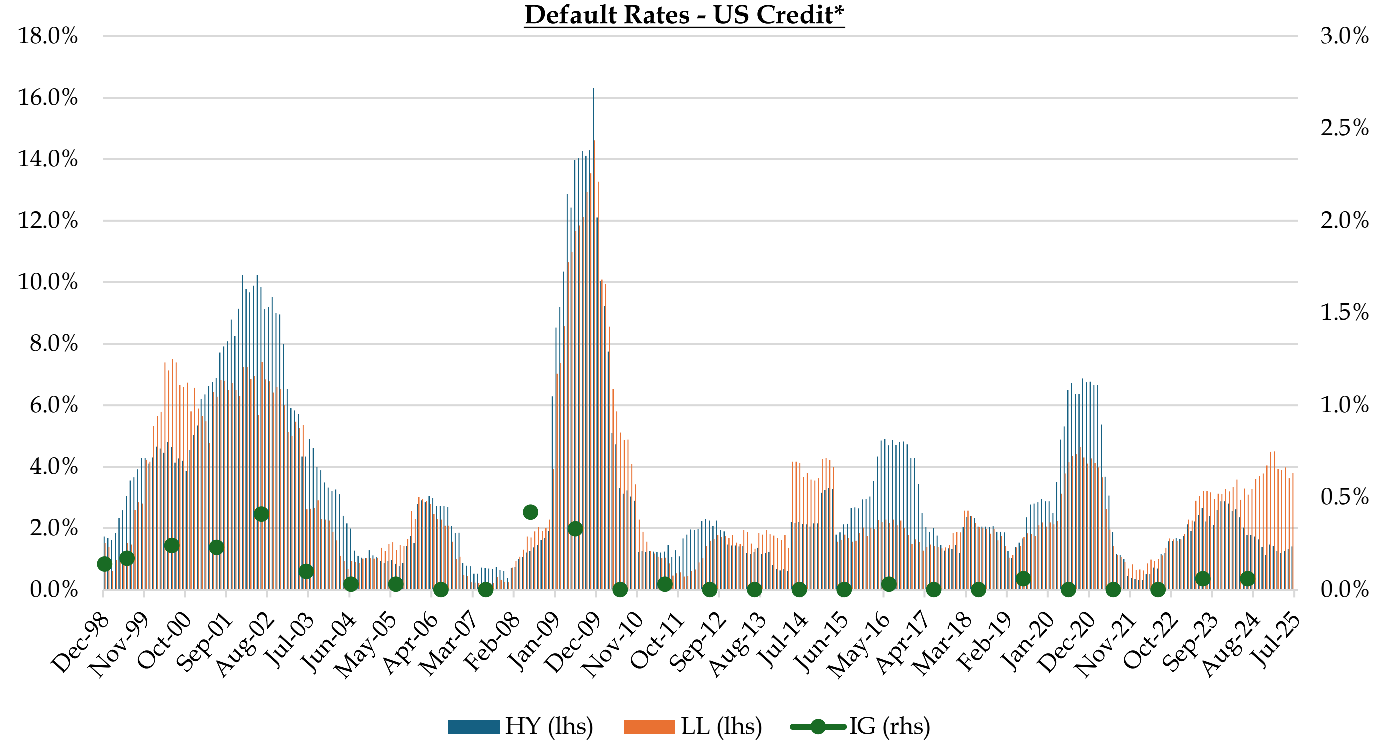
The Reg Cap sector spans a variety of reference assets and, of course, the performance of those assets varies among originators. Assets originated by banks to their clients for the banks' balance sheets have generally outperformed assets in generic credit indices. Further, investors impose selection criteria and originators, when selecting assets for a reference pool, are motivated to help ensure the success of their Reg Cap program on the most attractive terms. That said, we find it useful and important to track broad trends in asset performance in addition to deal-specific surveillance (which is non-public). Across the 40 investments that we own and track, referencing corporate, SME, middle market, consumer, and auto loans in Europe, North America, and Asia, we are seeing continued strong credit performance almost across-the-board, with just a few positions that we are monitoring more carefully due to slightly higher negative credit migration and/or default trends. The indices we look at as broadly representative of some of the most common reference assets include US Corporate Debt, including Investment Grade, High Yield and Leveraged Loans; European Investment Grade Debt and High Yield; and US Prime auto loans. We would expect most reference asset pools to significantly outperform these publicly available benchmarks. The following is a brief update on current credit trends for each.

US High Yield and Leveraged Loans

Most corporate credits in referenced pools are investment-grade quality. Defaults of investment grade obligors are rare. While Investment Grade ("IG") defaults have been only a small fraction of the defaults in leveraged credit (i.e. US High Yield "HY" bonds and Leveraged Loans "LL"), there is a strong correlation (~75%). Therefore, it is useful to track the (far more numerous) default activity in HY and LL as a possible bellwether for IG. Current default performance in HY and LL continues to be consistent with very low or no IG defaults.

There were no payment defaults in June in either bonds and loans, but activity in "liability management exercises," aka "LME" or "distressed" transactions reached a YTD high. Including LME, the par-weighted HY and LL default rates increased 8bp and 17bp MOM to 1.41% and 3.79%, respectively. The HY bond default rate remains near its November's multi-year low. The LL default rate has come down 70bp from its January's 4.5-year high and is expected to revert toward its 25-year average of 3.1%. The best bellwether for this is the size of the distressed trading universe, i.e. HY trading at spreads of 1000bp+ and LL trading at or below $80. Both show improvement. In LL, the percentage of loans trading at or below $80 fell to 5.1% in June, down from 5.3% in May and 6.2% in April (its recent peak). In HY, the percentage of bonds trading at spreads of 1000bp+ fell to 4.9% in June, down from 5.5% in May and 7.2% in April.

Default Rates - US Credit*



Source: Standard & Poor's, JPMorgan Research, as of July 1, 2025.
** HY and LL on a trailing 12-month basis, dollar-weighted. Includes distressed exchanges. IG on an annual basis.*

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Reg Cap Fundamental Credit Trends (Cont.)

European High Yield

Historically, IG defaults in Europe have also been very low, with no defaults at all in most years. Our European HY default data goes back to 2005. Since 2005, the default rate for IG in Europe has been zero in every year but two; in both 2008 and 2009 the IG default rate was 11bp per annum. Again, as with the US market, with so little default activity in IG, we turn to the HY market as a bellwether.

The trailing-12mo.default rate for European High Yield was 4.04% as of the end of June. While a 16bp MOM improvement, default rates remain elevated; for example, the year-ago level was 2.79%, 125bp lower than today. With new macroeconomic pressures, refinancing challenges given the jump in rates, and tariff impacts, defaults are expected to remain at or above today's level. Markets seem unconcerned, citing low leverage and robust interest coverage. While HY spreads spiked sharply in April's turmoil, spreads recovered quickly. As with risk markets elsewhere, the level of distressed European HY paper (defined as bonds trading at a spread of >= 1000bp) improved this month. The share of bonds trading wide of 1000bp dropped 116bps MOM to 4.92%, down 60bps MOM and to a three-year low.

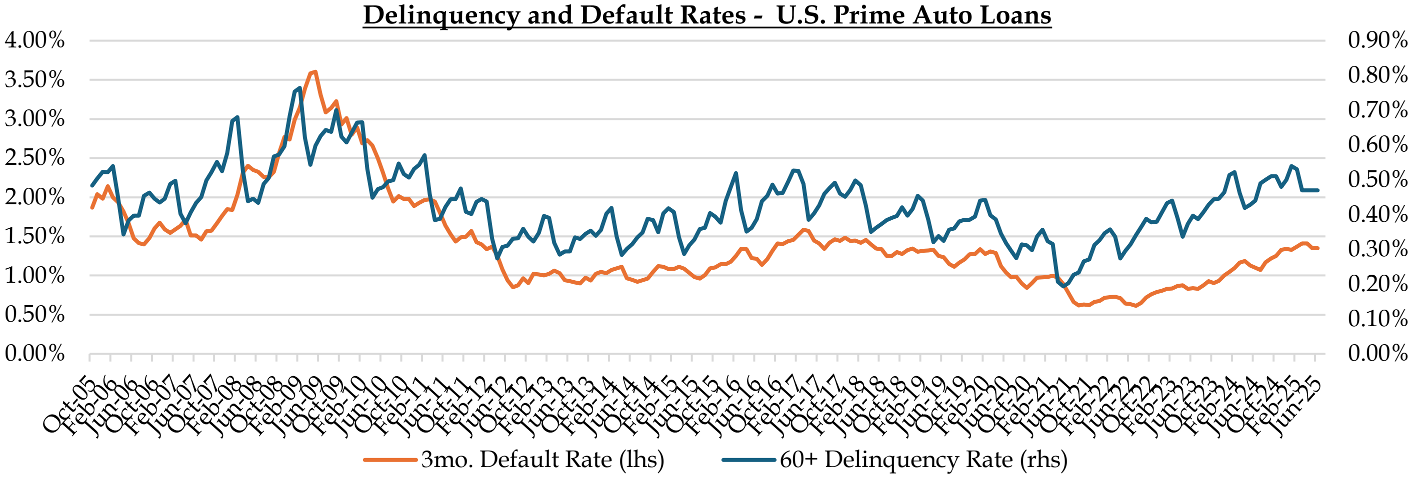
Default Rates - European High Yield

Source: JPMorgan Research, as of June 2025. Trailing 12-month basis, dollar-weighted. Excludes Banks/Insurers.

US Prime Auto Loans

The 60+ delinquency rate for securitized US Prime Auto Loans was flat MOM in June, at 47bp. The 3-month default rate was also unchanged MOM and stands at 135bp. Both metrics are moderately elevated vs. historical data. Auto delinquencies remain elevated and above the historicals, adjusting for seasonality. Many expect the macroeconomic headwinds could drive delinquencies higher over the next year, but the brunt of that is likely to be felt in subprime auto portfolios rather than prime ones. During the Great Financial Crisis, prime auto CDRs peaked briefly at 3.6% and then fell to 3%, about twice the rate we see today.

Delinquency and Default Rates - U.S. Prime Auto Loans



Source: Morgan Stanley, as of June 30, 2025

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Reg Cap News

Issuance News:

The new issue Reg Cap calendar is relatively light at the moment as 1) many banks scrambled to complete deals at the end of June to be reflected in 1H financials, and 2) European activity is typically slower during the summer holiday period, although we are seeing a number of processes kicking off.

Intesa Plans to Offload €13 Billion Risk Via SRT Deals This Year (Bloomberg News, aka "BN," 7/10/25)

Intesa, Italy's largest bank, plans to offload credit risk tied to about €13 billion of loans in 2025 by issuing SRTs. They are about halfway there already this year. The bank noted that "It's a very favorable moment for SRTs with abundant liquidity in the market and strong investor demand." Intesa is planning SRTs tied to a portfolio of revolving credit facilities, infrastructure and corporate loans. So far this year Intesa has already issued SRTs referencing US corporate loans, ESG loans, and SME under their GARC program. Intesa sees its common equity tier 1 ratio — a key metric of financial strength — rising to above 13.7% at the end of this year from around 13.3% at the end of 2024, in part due to the benefits of SRT issuance. At Seer, we note that Intesa is one of the few European banks trading above book value. Part of the driver of this is the bank's ability to effectively manage RWAs and risk using SRT.

UniCredit's SRT Boom Targets €20 Billion of Loans This Year (BN, 7/15/25)

Italy's UniCredit, a key player in a wave of industry consolidations, is ramping up the use of SRT (aka "Reg Cap") to free up capital. UniCredit is expected to issue SRTs tied to ~ €20 billion of loans this year, a ~30% YOY jump. Their Reg Cap activity this year has included deals tied to loan portfolios in Italy, Germany, Bulgaria, Romania and Croatia, and they are said to be exploring issuing SRT linked to project finance, commercial real estate and factoring. UniCredit has been a regular issue of SRTs since 2021, offloading the credit risk of at least €45bn cumulatively, by some estimates. UniCredit, is busily expanding its footprint domestically as well as in Germany and Greece. The use of Reg Cap has helped UniCredit to keep its "core equity tier 1" ratio consistently above 16%, as it does so. At Seer we note that Unicredit, in line with its crosstown rival Intesa, has been rewarded by the equity markets with a valuation above book value, partly in recognition of effective use of Reg Cap.

Aareal Bank, Erste Group Bank, Standard Chartered and ING Groep are among other banks currently discussing or finalizing Reg Cap deals.

Banking Industry News:

Deutsche Bank Says Basel Capital Rules to Crimp Defense Finance (BN, 7/2/25)

Deutsche Bank's top risk manager warned Europe against policies which he fears prioritize bank safety over defense, arguing that Germany regulators risk leaving a legacy that will be "unfortunately, they didn't have tanks, but the banking regulation was really fair." The DB executive told a Frankfurt banking conference that Europe's implementation of new global capital rules (Basel 3.1, which does not come fully into force until 2033), undermines banks' ability to support longer-term projects critical to defense.

He added that looming regulation is already affecting banks' lending decisions for smaller, unrated companies, some of which are critical suppliers to the defense industry and often need eight- to 10-year financing for large orders. With heightened geopolitical unrest, defense financing has become a hot topic in the EU. Moreover, bankers are asking that regulators be mindful of the need for a level playing field internationally, "especially if the US is now easing regulation." Deutsche Bank's shares recently came under pressure as investors worry about the impact of new capital requirements, though analysts claimed that the selloff was "an overreaction."

Modifications to the Capital Plan Rule and Stress Capital Buffer Requirement (FederalReserve.gov, 7/2/25)

The Board is inviting public comment on a notice of proposed rulemaking that would amend the calculation of the Board's stress capital buffer requirement applicable to certain large bank holding companies, The change is hoped to help reduce volatility in stress capital buffers. The proposal would average the results in each of the Board's prior two annual supervisory stress tests to determine a firm's stress capital buffer requirement. The proposal would also extend the annual effective date of the stress capital buffer requirement by one quarter, to provide additional time for firms to comply. Lastly, the proposal would make changes to the reports used to collect net income data with the goal of improving the accuracy of buffer calculations, as well as remove unneeded data requirements. The changes in the proposal are not designed to materially affect overall capital requirements but would ease reporting burdens.

Bundesbank Favors 'Radical' Capital Simplification for Lenders (BN, 7/3/25)

Bundesbank board member Michael Theurer highlighted ongoing efforts to reduce the regulatory burden on banks, including potential changes to stress tests, ESG reporting, and risk management standards, in his remarks at a recent banking conference in

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Reg Cap News (Cont.)

Germany. Theurer noted that European banks face a complex system of reserve requirements with national, EU, and global layers. Theurer advocated for simplifying capital buffers into what he called "releasable" and "non-releasable" types, which he claims could enhance transparency and efficiency. Meanwhile a high-level ECB task force is slated to propose capital-neutral reforms to streamline banking regulations by year-end.

Merz Signals Germany Won't Budge on Bank-Deposit Protection (BN, 7/3/25)
The ECB has been arguing in favor of a joint European Union deposit insurance scheme, which they believe would make the banking system stronger, and many bankers say is a precondition for cross-border mergers. However, German Chancellor Friedrich Merz is unconvinced and remains opposed. Merz also recently spoke out against a potential takeover of Frankfurt-based Commerzbank AG by Italy's UniCredit. Merz's comments against forming EU-wide deposit insurance were made to an audience of German banking executives, who have voiced concern that they could be on the hook for losses at lenders in other EU countries.

Post-Crisis Regulatory Reforms and the Decline of Securitization (Bank Policy Institute, 7/3/25)
The Bank Policy Institute argues that securitization provides more efficient financing for lenders which, in turn, drives expanded and less expensive access to credit for both households and businesses. However, U.S. securitization issuance activity remains well below pre-crisis levels, arguably at least in part due to the post 2008 regulatory environment, particularly Basel III reforms and Risk Retention rules. The U.S. Treasury previously recommended, in 2017, that regulators consider recalibrating certain aspects of these reforms to promote "a more vibrant and resilient securitization market." Under the new administration, the BPI advocates dusting off these recommendations to better support the securitization market, chiefly:

1. Recalibrating capital requirements
2. Streamlining risk-weight rules
3. Enhancing disclosure and transparency
4. Reassessing output floor effects to prevent overcapitalization for lower-risk, high-quality transactions.

The Securities That Banks Are Backing Away From (BN, 7/5/25)
Despite strong investor demand, U.S. banks are retreating from issuing preferred stock. JPMorgan cut its preferred outstanding by more than 25% last year, and Capital One's recently redeemed $500mn in preferred stock. The market has now shrunk for the second year in a row, despite strong investor appetite. Under new, eased Basel III regulation, banks have less incentives to issue preferred stock, especially given the high dividends they sport. At the same time, investors are pouring money into preferred funds, boosting their assets by over 10% this year.

Finance Watchdog Confronts Climate Discord After Officials Clash (BN, 7/8/25)
The Financial Stability Board (FSB) is dealing with disagreements among its members over how to handle climate-related financial risks, leading to changes in its upcoming report on the subject, according to sources. While many European countries are pushing for more action, others, especially the U.S., believe the current work is enough. The split became clear during a recent FSB meeting in Madrid and has resulted in more cautious language in the report. This comes as the G20, which the U.S. will lead next, has asked the FSB to give an update on its progress on the matter. The controversy highlights growing tensions over how climate change should be addressed in global financial oversight, if at all.

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About Seer

Seer Capital Management LP is a diversified, credit-focused investment firm founded by Phil Weingord in 2008 that primarily invests in structured credit and loans. We allocate capital opportunistically across all major asset classes within structured credit in the U.S. and Europe, including: bank regulatory capital risk transfer (SRT), residential and commercial mortgages, syndicated and SME loans, and a variety of consumer loans (personal, auto, credit card, student, housing). These investments are executed through active trading in both legacy and new issue securitizations, purchase and securitization of whole loans, and direct lending joint ventures.

Seer Capital believes it is well positioned to capitalize on opportunities in structured credit as a result of our highly experienced senior investment team, which has on average more than two decades of experience working in structured credit.

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