



High supply creating attractive opportunities in ABS

For professional investors only | Marketing communication

Securitized Credit team

Published October 2024

“European auto loan ABS bonds have long had the attractive characteristics of strong fundamentals, fast de-levering, likely upgrade potential, and short spread duration.”

European auto loan ABS bonds have long had the attractive characteristics of strong fundamentals, fast de-levering, likely upgrade potential, and short spread duration. In recent times an increase in supply has made the asset class even more appealing, with wider spreads and more deals to choose from. Technical opportunities such as this typically offer strong risk-adjusted value and now that supply/demand has re-balanced, we believe it’s an attractive entry point for Auto ABS across our strategies.

Why are we seeing high supply?

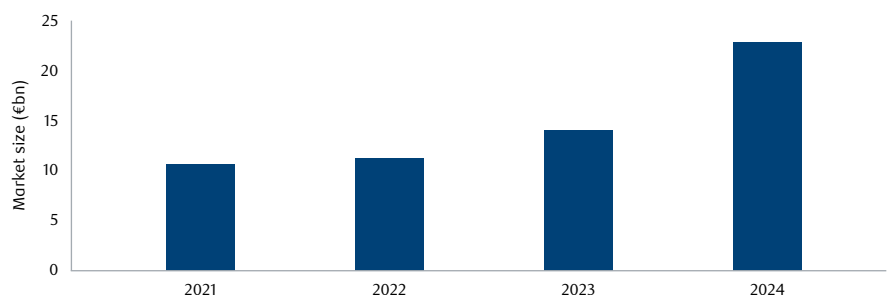
The increase in volume has been driven by four main factors:

1. Banks have had to move away from reliance on central banks for funding, and ABS markets need to fill the gap.
2. Beyond the need for funding, banks are seeking capital relief, which can be achieved by issuing ABS.
3. New non-bank lenders looking to diversify funding and enter the ABS market for the first time.
4. Consistent demand for loans from consumers despite continued strong lending standards.

What’s the impact?

The technical backdrop for the European ABS market has shifted, causing spreads to widen on new deals and creating attractive investment opportunities that we have already been taking advantage of. Looking at historic European consumer ABS supply, given the short-dated nature of the bonds (2-3 years), net supply is typically relatively low. However, elevated new issue volumes has shifted this dynamic and caused a softening in spreads.

Figure 1: Consumer ABS market size (€bn)



Source: Chart Consumer Loan ABS Market Size. Morgan Stanley, 4 October 2024.

Looking at a snapshot of the capital structure in new issue ABS and comparing to recent tights and similarly rated corporates, the attractive risk adjusted value on offer in European ABS is evident, with shorter WAL and higher spreads versus both recent tights and corporates.

Asset class	Rating	Current spread (bps)	2021 spread tights (bps)	Basis to tights (bps)	Spread duration
European ABS	A	160	95	+65	2.8 yrs
	BBB	200	135	+65	2.8 yrs
European Corporates	A	78	28	+50	4.8 yrs
	BBB	104	55	+49	4.4 yrs

Source: RBC BlueBay, Bloomberg, representative deal for European ABS, Indices for European Corporates ER30, ER40. Spread vs swaps, at 30 September 2024.

What are we doing?

This backdrop is attractive for our strategies as we are focused on seeking the best risk-adjusted returns and when issuance is high, it gives us a real opportunity to find bonds that are mispriced and offer attractive total returns, but without taking undue credit risk. We are always looking for technical dislocations, as opposed to fundamental deterioration, and as such we are positioned for it. We expect to see further opportunities in European ABS in the final quarter, as well as other areas of Securitized Credit which are experiencing similar trends.

“We are always looking for technical dislocations, as opposed to fundamental deterioration, and as such we are positioned for it.”

Reminder: the key features of ABS

- Yield pick-up and attractive risk adjusted spreads: ABS typically offer a higher yield versus similarly rated corporates alongside shorter spread duration.
- Limited exposure to single names: ABS have diversified asset pools, thus have extremely low sensitivity to single name credit risk.
- Default protection: ABS bonds are structured into layers of credit risk, with robust structures that absorb losses creating very high quality investment opportunities.
- Diversification: ABS offer exposure to differing types of risk; for example, consumer risk, which provides a diversifier versus common government and corporate risk.

This document is a marketing communication and it may be produced and issued by the following entities: in the European Economic Area (EEA), by BlueBay Funds Management Company S.A. (BBFM S.A.), which is regulated by the Commission de Surveillance du Secteur Financier (CSSF). In Germany, Italy, Spain and Netherlands the BBFM S.A is operating under a branch passport pursuant to the Undertakings for Collective Investment in Transferable Securities Directive (2009/65/EC) and the Alternative Investment Fund Managers Directive (2011/61/EU). In the United Kingdom (UK) by RBC Global Asset Management (UK) Limited (RBC GAM UK), which is authorised and regulated by the UK Financial Conduct Authority (FCA), registered with the US Securities and Exchange Commission (SEC) and a member of the National Futures Association (NFA) as authorised by the US Commodity Futures Trading Commission (CFTC). In Switzerland, by BlueBay Asset Management AG where the Representative and Paying Agent is BNP Paribas Securities Services, Paris, succursale de Zurich, Selnaustrasse 16, 8002 Zurich, Switzerland. The place of performance is at the registered office of the Representative. The courts at the registered office of the Swiss representative or at the registered office or place of residence of the investor shall have jurisdiction pertaining to claims in connection with the offering and/or advertising of shares in Switzerland. The Prospectus, the Key Investor Information Documents (KIIDs), the Packaged Retail and Insurance-based Investment Products - Key Information Documents (PRIIPs KID), where applicable, the Articles of Incorporation and any other document required, such as the Annual and Semi-Annual Reports, may be obtained free of charge from the Representative in Switzerland. In Japan, by BlueBay Asset Management International Limited which is registered with the Kanto Local Finance Bureau of Ministry of Finance, Japan. In Asia, by RBC Global Asset Management (Asia) Limited, which is registered with the Securities and Futures Commission (SFC) in Hong Kong. In Australia, RBC GAM UK is exempt from the requirement to hold an Australian financial services license under the Corporations Act in respect of financial services as it is regulated by the FCA under the laws of the UK which differ from Australian laws. In Canada, by RBC Global Asset Management Inc. (including PH&N Institutional) which is regulated by each provincial and territorial securities commission with which it is registered. RBC GAM UK is not registered under securities laws and is relying on the international dealer exemption under applicable provincial securities legislation, which permits RBC GAM UK to carry out certain specified dealer activities for those Canadian residents that qualify as “a Canadian permitted client”, as such term is defined under applicable securities legislation. In the United States, by RBC Global Asset Management (U.S.) Inc. (“RBC GAM-US”), an SEC registered investment adviser. The entities noted above are collectively referred to as “RBC BlueBay” within this document. The registrations and memberships noted should not be interpreted as an endorsement or approval of RBC BlueBay by the respective licensing or registering authorities. Not all products, services or investments described herein are available in all jurisdictions and some are available on a limited basis only, due to local regulatory and legal requirements.

This document is intended only for “Professional Clients” and “Eligible Counterparties” (as defined by the Markets in Financial Instruments Directive (“MiFID”) or the FCA); or in Switzerland for “Qualified Investors”, as defined in Article 10 of the Swiss Collective Investment Schemes Act and its implementing ordinance, or in the US by “Accredited Investors” (as defined in the Securities Act of 1933) or “Qualified Purchasers” (as defined in the Investment Company Act of 1940) as applicable and should not be relied upon by any other category of customer.

Unless otherwise stated, all data has been sourced by RBC BlueBay. To the best of RBC BlueBay’s knowledge and belief this document is true and accurate at the date hereof. RBC BlueBay makes no express or implied warranties or representations with respect to the information contained in this document and hereby expressly disclaim all warranties of accuracy, completeness or fitness for a particular purpose. Opinions and estimates constitute our judgment and are subject to change without notice. RBC BlueBay does not provide investment or other advice and nothing in this document constitutes any advice, nor should be interpreted as such. This document does not constitute an offer to sell or the solicitation of an offer to purchase any security or investment product in any jurisdiction and is for information purposes only.

No part of this document may be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, in whole or in part, for any purpose in any manner without the prior written permission of RBC BlueBay. Copyright 2024 © RBC BlueBay. RBC Global Asset Management (RBC GAM) is the asset management division of Royal Bank of Canada (RBC) which includes RBC Global Asset Management (U.S.) Inc. (RBC GAMUS), RBC Global Asset Management Inc., RBC Global Asset Management (UK) Limited and RBC Global Asset Management (Asia) Limited, which are separate, but affiliated corporate entities. ® / Registered trademark(s) of Royal Bank of Canada and BlueBay Asset Management (Services) Ltd. Used under licence. BlueBay Funds Management Company S.A., registered office 4, Boulevard Royal L-2449 Luxembourg, company registered in Luxembourg number B88445. RBC Global Asset Management (UK) Limited, registered office 100 Bishopsgate, London EC2N 4AA, registered in England and Wales number 03647343. All rights reserved.

Published October 2024

RE/0143/10/24



RBC BlueBay
Asset Management