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JSF the Journal of STRUCTURED FINANCE

Welcome to the Winter 2022 issue of *The Journal of Structured Finance*. Global securitization activity has been strong though 2021, exceeding the prior year's levels in almost all asset classes, despite the challenges of the Covid-19 pandemic. Notably, the brisk activity in 2021 included record setting levels of agency RMBS issuance.

The new year opens amidst an environment of mixed signals. On the positive side, household balance sheets are quite strong, having received a solid boost from pandemic-related relief programs. Additionally, the unemployment rate is low, hinting at strength in the labor market. On the other hand, inflation is starting to appear and may pose a significant risk for 2022 and beyond. According to one view, the current inflationary environment is most likely temporary (Alpert 2021). However, the federal debt now exceeds $29 trillion, amounting to significantly more than the nation's annual GDP (Exhibit 1). Just the interest on the debt amounts to more than $400 billion annually. Also, the Fed's balance sheet is nearly $9 trillion. These are potential sources of long-term inflationary pressure. Indeed, the federal debt is already so large that the oft-quoted amount of $1.7 trillion for the Biden Administration's proposed "Build Back Better" program seems reasonably modest. What this all amounts to is uncertainty as we enter 2022.

Another issue is US home prices (Exhibit 2). Home prices have been firmly outpacing inflation since roughly 2014, gaining about 5% each year. However, their advance during 2021 has been exceptional. This suggests at least the possibility of a correction, as occurred following the mid-2000s home price bubble. One thing is clear though. If there is a new home price bubble, it was not caused by easy lending in the non-agency space. The agencies are simply too dominant for non-agency mortgage activity to be a key driver of overall market trends.

This issue opens with an article on US infrastructure finance by Barry Gold, the head of Marathon Capital Partners, and Allan Marks, a partner at Milbank. They address recent developments in the US infrastructure sector and explain several myths about infrastructure that lead to misunderstanding the sector. The article is timely because of the recent focus on infrastructure and the enactment of the Infrastructure Investment and Jobs Act.[1]

The second article discusses the Supreme Court's decision in *Collins v. Yellen*. Alex Malyshev, a partner at Carter Ledyard & Milburn, explains how the Supreme Court extended its reasoning from an earlier decision to hold that the original structure of the FHFA—with a single director insulated from removal at will by the President—violated the Constitution. However, the Court also held that, despite the Constitutional defect in its structure, the FHFA's action in agreeing to sweep all the profits from Fannie Mae and Freddie Mac to the US Treasury was valid.

The issue's third article is by Yini Yang, Joy Zhang, and David Zhang, all of whom are in securitized product research at MSCI. They examine the benefit of using loan-level data on auto loans to improve projections of defaults on auto loan ABS.

[1] Infrastructure Investment and Jobs Act, Pub. Law No. 117-58, 135 Stat. 429 (2021), https://www.congress.gov/117/bills/hr3684/BILLS-117hr3684enr.pdf. The act was signed into law on November 15, 2021.

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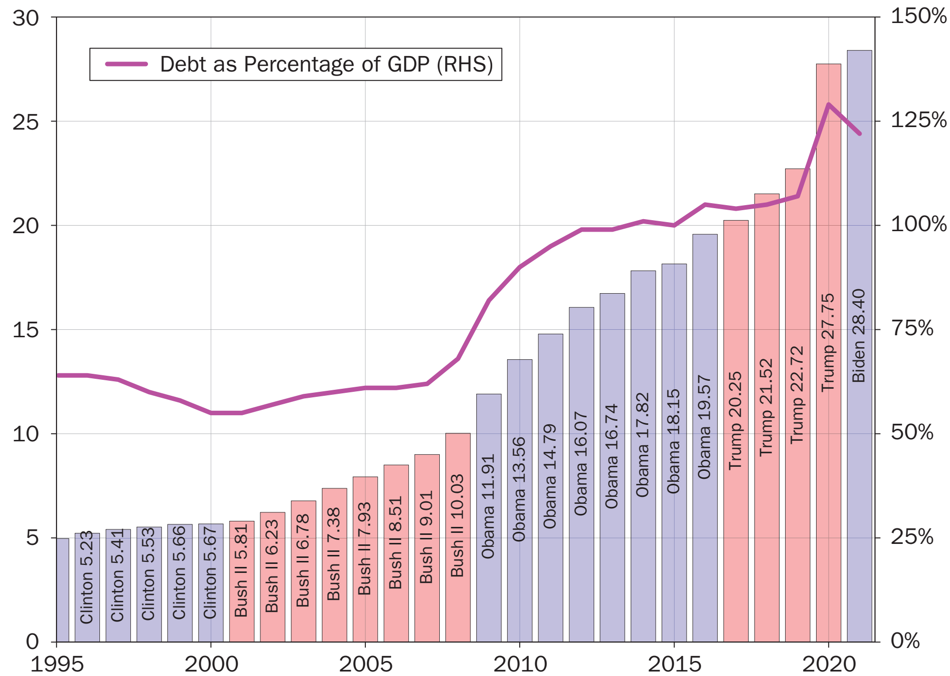
EXHIBIT 1

US Federal Debt ($ trillions)

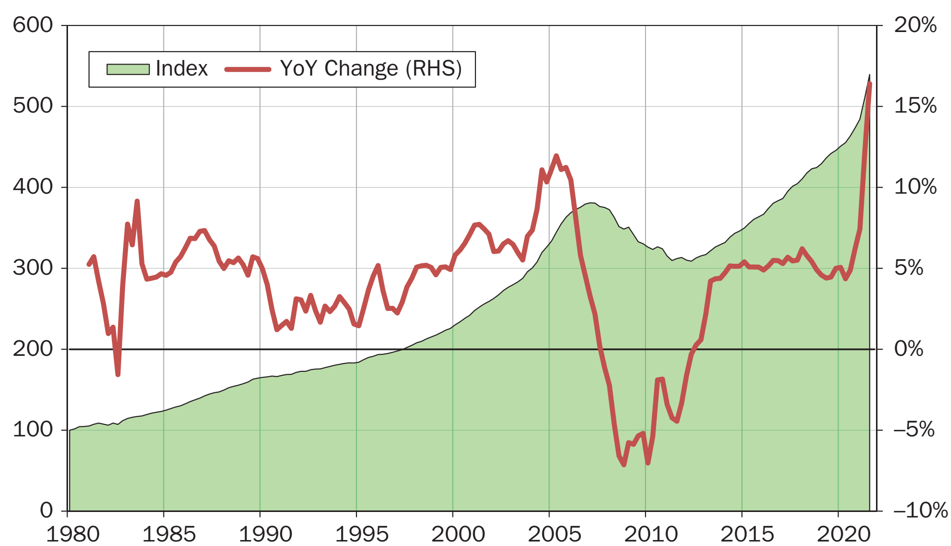


NOTE: Values for 2021 are as of the end of Q3.

SOURCE: The Balance, https://www.thebalance.com/national-debt-by-year-compared-to-gdp-and-major-events-3306287.

EXHIBIT 2

FHFA US Home Price Index (all transactions, quarterly)



NOTE: Data through 2021Q3.

SOURCE: FHFA.

They conclude that using loan-level data substantially improves predictions. They show that vehicle type, loan-to-value ratio, gross coupon, term, issuer, loan age, and subvention are important drivers of credit performance. They demonstrate that models using those data items can substantially improve loan default projections.

The next item is by Reed Auerbach, Susan DiCicco, and David Monteiro, all of whom are partners at Morgan Lewis. They discuss the "true lender" issue and the associated OCC rule[2] that Congress invalidated[3] by applying the Congressional Review Act.[4] Invalidating the rule creates uncertainty about whether state consumer protection laws, such as usury limitations, apply to lending activities by fintech lenders across state lines. The article provides background on the issues and explains case law developments around it.

The next item is my report on the recent 27th Annual ABS East Conference at the Fontainebleau in Miami Beach. The report covers 18 sessions, including the general sessions on Tuesday and breakout sessions covering ESG, the pandemic, mortgage-backed securities, consumer ABS, equipment lease ABS, and aircraft ABS.

Following the report on the ABS East Conference are selected highlights from *GlobalCapital* for the fourth quarter of 2021. The selection was compiled and curated by *GC* securitization editor Jennifer Kang. It includes five important stories. The first discusses the transition to SOFR from LIBOR and how legislation is helping the process in the US. The second examines the implications of Hertz's order for 100,000 electric vehicles from Tesla. The third explains how the strength of the CLO market during 2021 caused the ranks of CLO managers to swell. The fourth discusses Fannie Mae's CAS 2021R1 deal, which was the GSE's first credit-risk-transfer transaction after a long dry spell. The fifth discusses challenges that the US CLO market will face in early 2022, including the effects of using SOFR on the pricing of both debt and equity classes.

This issue also includes a selection of industry news items from the Structured Finance Association, also from Q4 2021. The section includes more than two dozen snippets covering a wide range of developments during the year's fourth quarter.

As always, we welcome your submissions. Please encourage those you know who have good papers or who have made good presentations on structured finance- or project finance-related subjects to submit them to us.

Submission guidelines can be found at https://jsf.pm-research.com/authors. If you have comments or suggestions, you can e-mail them directly to me at m.adelson@pm-research.com.

REFERENCE

Alpert, D. 2021. "Inflation in the 21st Century: Taking Down the Inflationary Straw Man of the 1970s." Cornell Research Academy of Development, Law, and Economics and Mario Einaudi Center for International Studies. October. https://scholarship.law.cornell.edu/facpub/1740/.

Mark Adelson
Editor

[2] 12 C.F.R. § 7.1031 (2021); Office of the Comptroller of the Currency, *National Banks and Federal Savings Associations as Lenders*, 85 Fed. Reg. 68742 (Oct. 30, 2020).

[3] Pub. Law No. 117-24, 135 Stat. 296 (June 30, 2021).

[4] 5 U.S.C. §§ 801–808 (2019).