

Esoteric ABS Strategy Fact Sheet

December 2023

ASSET MANAGEMENT | FACT SHEET

Conning believes that Esoteric ABS is a compelling asset class in today's market. Esoteric ABS typically offer higher yields than similarly rated corporate bonds and other structured products. The asset class also provides strong capital preservation through structural protections. Historically, Esoteric ABS have proven to be extremely resilient through multiple market cycles.

In addition, Esoteric ABS offer diversification benefits through negative correlation to U.S. Treasury bonds and low correlations to U.S. investment grade (IG) corporate bonds.

ABS Credit Loss Rates During the Great Financial Crisis

Peak Credit Loss Rates		
	ABS	Non-Agency RMBS
AAA	0 %	6.5%
AA	0 %	40.8%
A	1.2 %	45.2%
BBB	1.7 %	57.2%

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Team

Michael Nowakowski
Head of Structured Products
16 years of experience

Esoteric ABS Overview

Assets backing Esoteric ABS are less well-known than typical ABS collateral such as credit card receivables. Esoteric ABS are not issued on a regular basis and deal sizes can be smaller than typical ABS offerings. However, Esoteric ABS structures are similar to other ABS structures with a senior class and some form of credit enhancement, usually in the form of subordination, overcollateralization, excess spread, etc. Conning segregates Esoteric ABS into two major types: Commercial and Consumer.

Commercial securities are backed by equipment including commercial jets, shipping containers and rail car boxes. The underlying equipment is contributed by the issuer, usually leasing companies such as Triton or Air Lease, which rent equipment to firms like Southwest, Chiquita, Cargill, Exxon Mobil, Tyson Foods and others.

Consumer securities are backed by loans from a variety of sources, such as timeshares, subprime auto loans, and a variety of unsecured loans. The underlying receivables are contributed by the issuer, typically a non-bank lender like Marriott or Dell, whose loans to consumers are generally outside traditional bank channels.

Benefits of Investing in Esoteric ABS

- » **Attractive Yields** – Opportunity for incremental yield relative to similarly rated corporate bonds.
- » **Low Historical Defaults** – Low defaults overall and zero for AAA or AA ABS during the 2008-9 financial crisis.
- » **Shorter Durations** – Limited spread duration can help protect investors during market turbulence.
- » **Diversification** – Esoteric ABS have a lower correlation to IG corporate bonds and equities.
- » **Liquid Market** – Esoteric ABS typically trade with a bid/offer spread of 10 basis points – similar to corporates.
- » **Rating Upgrades** – The amortization of ABS structures may lead to rating upgrades over the life of the deal.

Investable Universe	
Esoteric ABS Sub-Sectors	Amount Outstanding
Consumer	
Subprime Auto	\$79.4 B
Consumer Loan	\$38.9 B
Solar	\$14.4 B
Structured Settlement	\$5.1 B
Royalties	\$3.4 B
Timeshare	\$5.8 B
Commercial	
Equipment Leases	\$35.8 B
Aircraft	\$21.8 B
Data Center	\$13.7 B
Wireless Tower	\$13.7 B
Container	\$10.8 B
Fiber	\$7.2 B
Rail	\$6.7 B
Total	\$256.7 B

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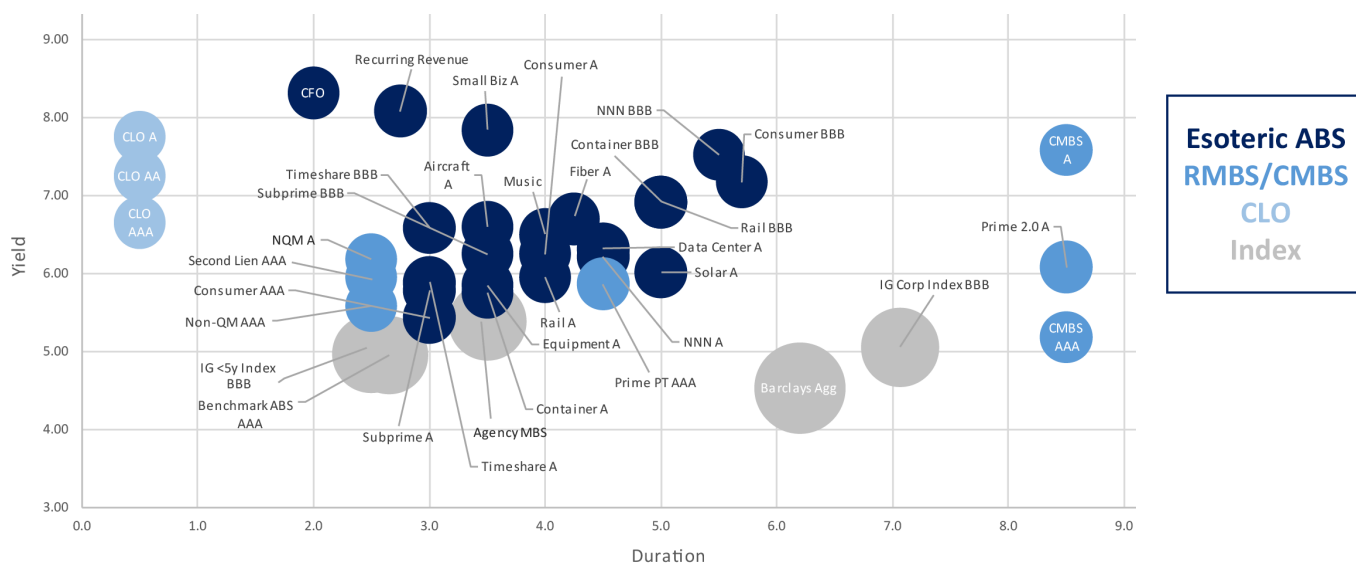
Esoteric ABS – Liquidity

Size and Liquidity Comparison		
Sub-Sector	Typical Size Per Deal	Typical Size Per Trade
ABS-Esoteric	\$250 – \$800 mm	\$250 K – \$10 mm
ABS-Auto	\$500 mm – \$1 B	\$250 K – \$10 mm
ABS-Student Loan	\$250 mm – \$1 B	\$250 K – \$10 mm
BBB-Corporate Bond	\$800 mm	\$1 mm – \$10 mm

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- » ABS market has proven to be highly liquid
- » Esoteric ABS have been a major component of dealer inventories
- » Trade size accommodates smaller and larger investors
- » Consistent TRACE volumes enhance price discovery

Esoteric ABS – Relative Value



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As of December 31, 2023

The Conning Advantage

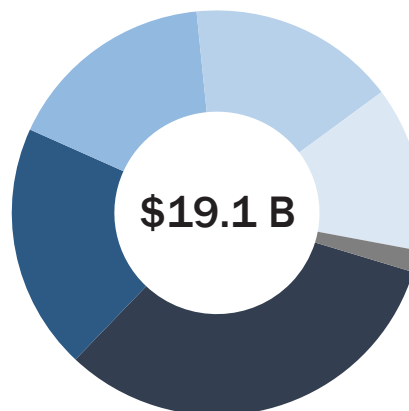
Asset Class Expertise

- » Team depth & focus
- » Credit research expertise
- » Structural expertise
- » Experience managing through multiple cycles

Enhanced Portfolio Management

- » Excellent access to trade flow and new issues
- » Proprietary systems and data dedicated to Esoteric ABS
- » Quantitative team analyzes non-commercial data

Conning Structured Assets Under Management¹



- 32.4% Mortgage-Backed Securities
- 19.6% CLO Debt
- 16.7% Asset-Backed Securities
- 16.4% Collateralized Mortgage Obligations
- 13.2% Commercial Mortgage-Backed Securities
- 1.7% CLO Equity

Prepared by Conning, Inc.

¹As of December 31, 2023, represents the combined global assets under management for the affiliated firms under Conning Holdings Limited.

Considerations for Insurers

Ratings

Esoteric ABS are rated by at least one major rating agency (i.e., S&P, Moody's, Fitch, Kroll, DBRS).

Pricing

Esoteric ABS are typically priced daily, including Reuters, IDC (Interactive Data Corp.), and Pricing Direct (JPM).

Accounting Classification

Rated Esoteric ABS tranches are debt securities and can be classified as trading, available-for-sale (AFS), or held-to-maturity (HTM).

Trade / Settlement Conventions

Standard three-day settlement for secondary market purchases; primary market purchases settle trade date plus one week.

Regulatory Capital Treatment

Highly rated Esoteric ABS tranches (i.e., AAA, AA, A) are considered NAIC 1-rated assets and benefit from the most favorable statutory capital charges.

Taxation

AAA, AA, A, and BBB Esoteric ABS tranches are debt for U.S. tax purposes and are taxed similarly to other debt instruments such as corporate bonds.

Investment Guidelines

Insurers should review applicability under existing guidelines and, if not permitted, investment committee approval may be required prior to investing in the asset class. For example, investment guidelines may have broad limitations on securitized asset classes, or limitations applicable to foreign country allocations.

Esoteric ABS Risk Factors (Include But Are Not Limited To)

Structure – Esoteric ABS often involve risks that differ from those associated with other types of debt instruments. The complex structure of the security may produce unexpected investment results not based on default or recovery statistics. Ratings agencies may downgrade their original ratings of Esoteric ABS debt tranches.

Valuation

Valuation of structured credit products is provided by third parties based on models, indicative quotes, and estimates of value, in addition to historical trades. There can be no assurances the assets can be disposed of or liquidated at the valuations established.

Default

During periods of economic uncertainty and recession, the incidence of modifications and restructurings of investments may increase, resulting in impairments to the underlying asset value and reduced subordination.

LIBOR

There is uncertainty with respect to the replacement of LIBOR with proposed alternative reference rates and it is possible that different markets might adopt different rates, or adopt replacement rates at different times, the effects of which are uncertain at this time and could include increased volatility or illiquidity.

General Market & Economic Conditions

Changing economic, political, regulatory or market conditions, interest rates, general levels of economic activity, the price of securities and debt instruments and participation by other investors in financial markets may affect the value of Esoteric ABS and all other asset classes.

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