STRUCTURED CREDIT: INTERESTING INVESTMENTS FROM FAST FOOD TO CLOUD COMPUTING

March 2025

Asset-backed securities (ABS)[1] may offer investors an interesting opportunity to access credit spreads.[2] In fact, some of these potential investment opportunities may be found in specialty sectors that fall outside of the traditional Bloomberg Aggregate Bond Index (Agg). Two areas of particular interest to our team include data centers and whole business securitizations (WBS).[3]

1 We believe ABS may offer investors an interesting opportunity to access high yield and high credit spreads, especially in less traditional sectors.

2 The demand for data centers is growing with the rapid rise of artificial intelligence (AI), presenting potential opportunities in digital infrastructure.

3 WBS offers another less traditional area for structured credit with the growth of fast food franchises, childcare brands and gyms, to name a few.

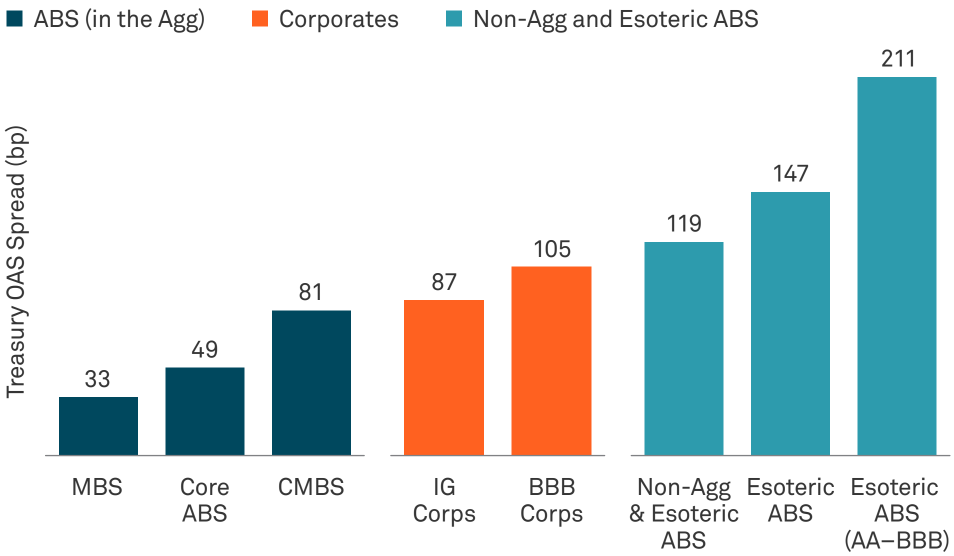
ABS may be an option for those seeking high yields and high spreads

ABS or asset-backed securities are financial securities funded by income-generating assets such as credit card debt, home equity loans, student loans and auto loans.

Today, fixed income investors are enjoying historically high yields but are contending with historically tight credit spreads, making it challenging to see meaningful relative returns.[4] However, ABS may offer investors the potential mix of high yield and high spreads. We see the most intriguing spread opportunities outside of the Agg, particularly in less traditional, or specialty "esoteric" ABS sectors.

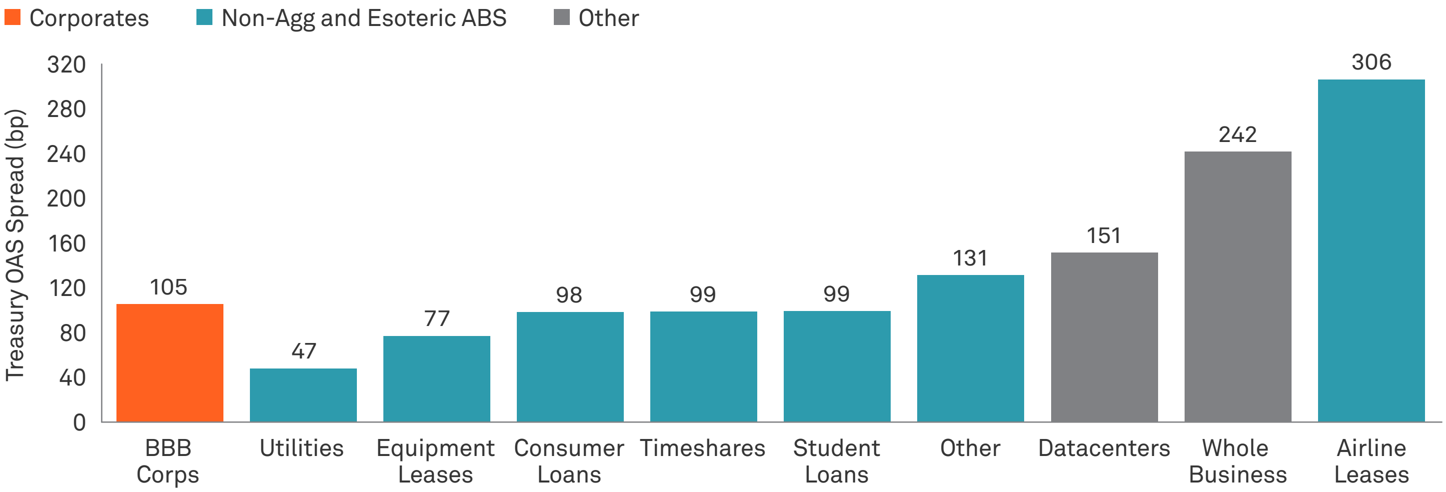
Esoteric ABS refers to investments with innovative or complex structures or those collateralized against nontraditional assets. Many esoteric deals may only be offered to a select set of investors. Their spread premium reflects complexity rather than additional credit risk, as credit ratings typically range from AAA to BBB. Among esoteric ABS, we believe there are potential opportunities within data centers and whole business securitization (see chart at the top of the following page).

STRUCTURED CREDIT MAY POTENTIALLY OFFER A YIELD PREMIUM OVER CORPORATE BONDS, DESPITE TYPICALLY HIGHER CREDIT RATINGS[5]



Past performance is not indicative of future results. Charts are for illustrative purposes only.

ESOTERIC STRUCTURED CREDIT MAY POTENTIALLY OFFER A SUBSTANTIAL "COMPLEXITY PREMIUM"[6]



Past performance is not indicative of future results. Charts are for illustrative purposes only.

Data centers – the digital age is not just an equity story

As the world braces for a potential "AI revolution,"[7] digital infrastructure (which includes data centers, cell towers and fiber-optic cables) is hungry for finance. The structured credit market may be playing a key role.

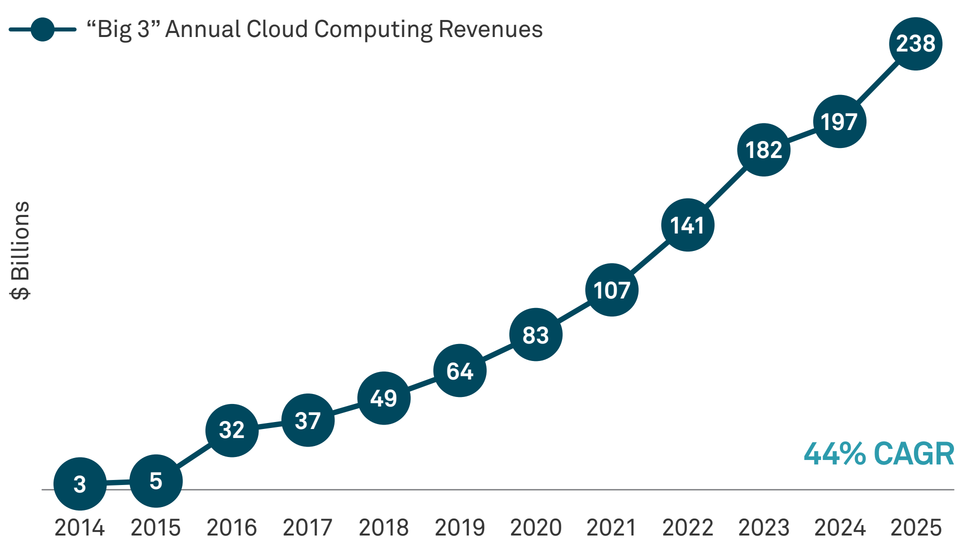
Data centers are the backbone of the internet. The "cloud" is in fact a network of physical facilities that store, process and distribute millions of gigabytes per second. They make technologies like 5G, big data, real-time analytics and video streaming possible.

Cloud computing has been a key driver of the data center build-out in recent years. As 89% of large businesses embark on digital and AI transformations, migrating in-house computing systems to cloud providers has become a key step.[8] Companies can lease anything from data center shelf space (known as retail "colocations") to entire buildings (known as "hyperscale" data centers). ABS deals tend to be secured against leases from multiple tenants and other assets while CMBS deals tend to be secured against a single borrower's mortgage on a hyperscale property.

The next phase of investment is being driven by computationally hungry generative AI systems like ChatGPT. For example, the Trump administration's "Stargate" initiative explicitly seeks private data center finance for AI development.[10] Energy generation may be a limiting growth factor but could still bode well for ABS investors given potential for rising rental premiums.

Notably, however, the development of China's competitor model DeepSeek raised questions on whether generative AI programs can run more efficiently than previously thought, negating some of the investment needed around data centers and the energy to power them. If it is the case, we believe it would impact newer properties, particularly those in areas with questionable energy infrastructure. Our focus is instead on areas with well-established leases and infrastructure — particularly North Virginia, the undisputed "data center capital of the world" with over four times as much data center inventory, and an advanced fiber optic infrastructure network.[11]

DEMAND FOR DATA CENTERS HAS BEEN GROWING[9]



Past performance is not indicative of future results. Charts are for illustrative purposes only. The Big 3 = Amazon Web Services (AWS), Microsoft Azure and Google Cloud Computing. CAGR = Compound Annual Growth Rate.

Whole business securitizations – franchising fixed income cash flows

WBS securitize most, if not all, of a company's (or single business line's) cash-generating assets.

The most natural issuers have been large franchises, as the regular fees that franchisees pay their franchisor are the type of cashflows that fixed income investors value. The most common issues have been fast-food industry giants, from sandwiches to pizza delivery.

In fact, America's top three food franchises all have WBS outstanding.[12] The current "number two" ranked franchise is Jersey Mike's, which has wrestled significant market share from its direct competitors. It issued a potentially attractive WBS in December backed by assets like franchisee fees and its US trademarks and priced much wider compared to equivalently rated corporate bonds.[13] In our view it benefits from strong debt metrics and strong private equity sponsor while retaining the services of its decades-long-standing CEO.

WBS can also encompass other businesses like gyms or childcare brands and even more unusual assets like media rights, as seen in a recent music copyright deal last August backed by royalty payments on songs from Bob Dylan, Adele and Neil Diamond.

Conclusion

Investors seeking diversification could potentially find interesting opportunities in structured credit, from data centers to restaurant chains. We believe a core plus strategy has the potential to offer attractive yields through exposure to securitized sectors and may provide a way for investors to add value to their portfolio by being intentional with their approach to ABS.

Learn more about Insight's investment capabilities, philosophies and solutions: **Getting to Know Insight Investment**.

INVESTMENT VIEWS FROM INSIGHT INVESTMENT

Insight Investment is a leading global investment manager and fixed income specialist firm within BNY Investments.

[1] Asset-backed securities (ABS) are financial securities backed by income-generating assets such as credit card receivables, home equity loans, student loans, and auto loans.

[2] A credit spread, also known as a yield spread, is the difference in yield between two debt securities of the same maturity but different credit quality.

[3] Whole business securitization (WBS) is a specialized securitization where a company's entire business operations and assets are bundled together and transformed into securities.

[4] Bloomberg, Insight, February 2025.

[5] Bloomberg, ICE, Insight, February 2025. OAS = Option adjusted spread; Core ABS = Bloomberg US ABS Index, ICE BofA US ABS, MBS = Bloomberg US Mortgage-Backed Securities (MBS) Index, CMBS = Bloomberg US CMBS: ERISA Eligible Index, BBB Corporates = ICE BofA BBB US Corporate Index, Esoteric ABS = ICE BofA US Fixed Rate Miscellaneous Asset Backed Securities Index, Esoteric ABS AA-BBB = ICE BofA AA-BBB US Fixed Rate Index. Please see index descriptions at the back of the document.

[6] Bloomberg, ICE, Insight, February 2025.

[7] Artificial Intelligence (AI) refers to computer systems that can perform tasks typically requiring human intelligence, such as visual perception, speech recognition, decision-making, and language translation.

[8] McKinsey, March 2024.

[9] Bloomberg, Insight, February 2025. Big 3: Amazon Web Services (AWS), Microsoft Azure and Google Cloud Computing.

[10] The Stargate initiative, announced by President Trump in 2025, calls for several major technology companies to invest at least $500 billion in artificial intelligence and data centers at a number of US locations.

[11] CBRE, North America Data Center trends, August 2024.

[12] Entrepreneur Franchise 500 Report, as of March 2025; rankings based on cost, size, growth and brand. The mention of a specific security is not a recommendation to buy or sell such security. The specific securities identified are not representative of all the securities purchased, sold or recommended for advisory clients. It should not be assumed that an investment in the securities identified will be profitable. Actual holdings will vary for each client and there is no guarantee that a particular client's account will hold any or all of the securities listed.

[13] Bloomberg, December 2024.

basis and to repay principal upon maturity. **Equities** are subject to market, market sector, market liquidity, issuer, and investment style risks to varying degrees.

Mortgage-Backed Security (MBS) is an investment similar to a bond that is made up of a bundle of home loans bought from the banks that issued them. Investors in MBS receive periodic payments similar to bond coupon payments. **Asset-Backed Security (ABS)** is a financial security such as a bond or note which is collateralized by a pool of assets such as loans, leases, credit card debt, royalties, or receivables. **Commercial mortgage-backed securities (CMBS)** are fixed-income investment products that are backed by mortgages on commercial properties rather than residential real estate. **Option Adjusted Spread (OAS)** is the measurement of the spread of a fixed income security rate and the risk-free rate of return, which is then adjusted to take into account an embedded option. **Core-plus strategies** are investment funds that primarily invest in investment-grade US fixed-income issues, but can also include noncore sectors.

Asset class comparisons such as comparing equities to bonds have limitations because different asset classes may have characteristics that materially differ from each other. Because of these differences, comparisons should not be relied upon solely as a measure when evaluating an investment for any particular portfolio. Comparisons are provided for illustrative purposes only. Although stocks have greater potential for growth than bonds, they also have much higher levels of risk. With stocks, the prices can rise and fall for a variety of reasons, including factors outside of the company's control. Bonds may be considered relatively safer. Because they're a debt security, they function as an IOU. The company pays interest to the bondholder, and once the bond matures, the bondholder receives the principal bank. Bonds aren't completely risk-free; there is the possibility of the issuer defaulting on its bonds, and if sold prior to maturity the market value may be higher or lower than the purchase value. But compared to stocks, historically there's been less volatility.

The Bloomberg Aggregate Bond Index is a broad-based fixed-income index used by bond traders and the managers of mutual funds and exchange-traded funds as a benchmark to measure their relative performance. **The ICE BofA US Mortgage-Backed Securities Index** measures market performance of US mortgage-backed securities. **The ICE BofA US Asset Backed Securities Index** measures market performance of US asset backed securities. Indexes are service marks of Bloomberg Finance L.P. and its affiliates, including Bloomberg Index Services Limited ("BISL"), the administrator of the index (collectively, "Bloomberg") and have been licensed for use for certain purposes by BNY. **The Bloomberg US Corporate Index** measures the investment grade, fixed-rate, taxable corporate bond market. **The Bloomberg US Corporate High Yield Bond Index** measures the USD-denominated, high yield, fixed-rate corporate bond market. **The Bloomberg CMBS: ERISA Eligible Index** measures the market of US Agency and Non-Agency conduit and fusion CMBS deals. **The Bloomberg US ABS Index** is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index only includes ABS securities. **The Bloomberg US Mortgage Backed Securities (MBS) Index** tracks fixed-rate agency mortgage backed pass-through securities guaranteed by Ginnie Mae, Fannie Mae, and Freddie Mac. **The Bloomberg US CMBS Investment Grade Index** measures the market of US Agency and Non-Agency conduit and fusion CMBS deals. **The ICE BofA BBB US Corporate Index** is a subset of the ICE BofA US Corporate Master Index that tracks the performance of investment grade corporate debt in the US. **The ICE BofA US ABS and CMBS Index** tracks the performance of investment grade asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS) in the United States.

Bond ratings reflect the rating entity's evaluation of the issuer's ability to pay interest and repay principal on the bond on a timely basis. Bonds rated BBB/Baa or higher are considered investment grade, while bonds rated BB/Ba or lower are considered speculative as to the timely payment of interest and principal. Credit ratings reflect only those assigned by Nationally Recognized Statistical Rating Organizations (NRSRO) that have rated fund holdings. Split-rated bonds, if any, are reported in the higher rating category.

This material has been provided for informational purposes only and should not be construed as investment advice or a recommendation of any particular investment product, strategy, investment manager or account arrangement, and should not serve as a primary basis for investment decisions. Prospective investors should consult a legal, tax or financial professional in order to determine whether any investment product, strategy or service is appropriate for their particular circumstances.

Views expressed are those of the author stated and do not reflect views of other managers or the firm overall. Views are current as of the date of this publication and subject to change. This information may contain projections or other forward-looking statements regarding future events, targets or expectations, and is only current as of the date indicated. There is no assurance that such events or expectations will be achieved, and actual results may be significantly different from that shown here. The information is based on current market conditions, which will fluctuate and may be superseded by subsequent market events or for other reasons. References to specific securities, asset classes and financial markets are for illustrative purposes only and are not intended to be and should not be interpreted as recommendations. Information contained herein has been obtained from sources believed to be reliable, but not guaranteed. No part of this material may be reproduced in any form, or referred to in any other publication, without express written permission.

Statements are current as of the date of the material only. Any forward-looking statements speak only as of the date they are made, and are subject to numerous assumptions, risks, and uncertainties, which change over time. Actual results could differ materially from those anticipated in forward-looking statements. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment and past performance is no indication of future performance.

BNY Investments is one of the world's leading investment management organizations, encompassing BNY's affiliated investment management firms and global distribution companies. BNY is the corporate brand of The Bank of New York Mellon Corporation and may be used to reference the corporation as a whole and/or its various subsidiaries generally.

Insight North America LLC is associated with other global investment managers that also (individually and collectively) use the corporate brand Insight Investment and may be referred to as "Insight" or "Insight Investment." Insight and BNY Mellon Securities Corporation are subsidiaries of BNY.

Investments: Not FDIC-Insured. Not Bank-Guaranteed. May Lose Value.

MARK-704478-2025-03-14

BNY | INVESTMENTS