



# SCI Annual Seminar

## Credit Market Dislocation



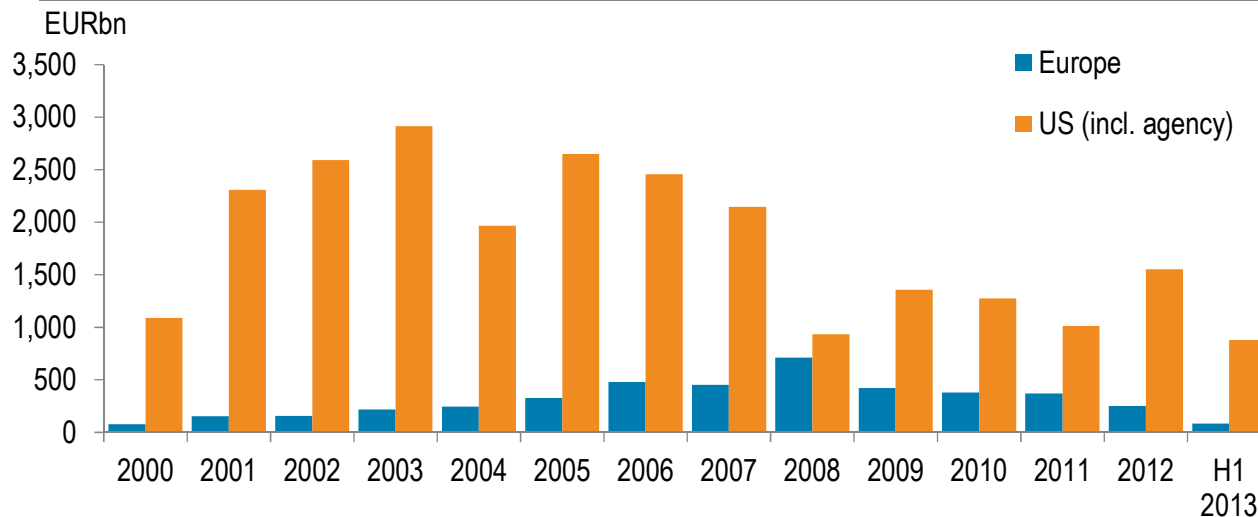
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4 December 2013

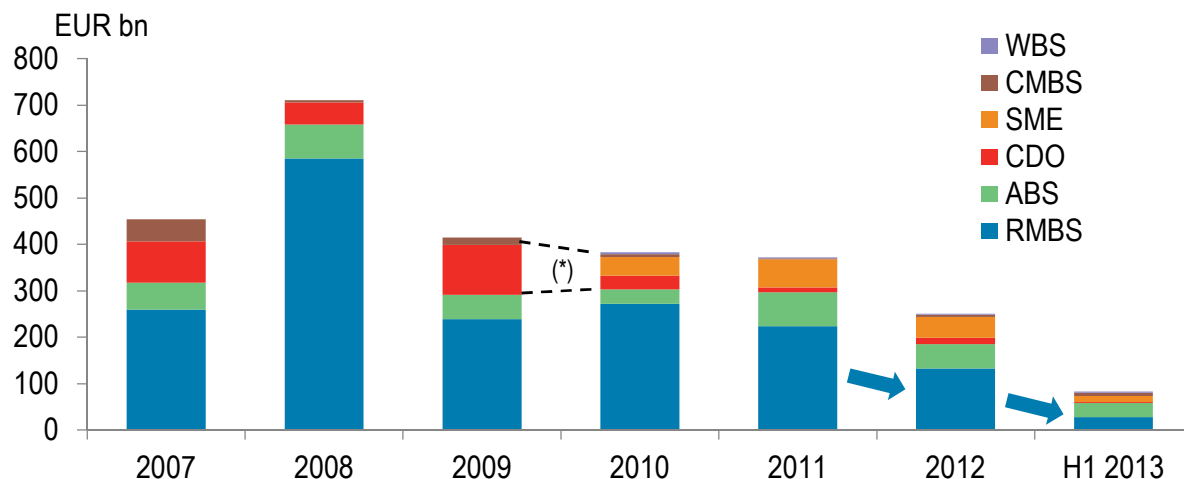
# Primary Securitisation Market Overview

## Global primary issuance volumes



- **Steady** issuance in the **US**
- **Sluggish** issuance in **Europe**

## European securitisation issuance volumes by asset class



(\*) SME are classified as CDO before Q2 2010

- **Substantial drop** in **RMBS** issuance (~50% y/y drop for the last 2 years)
- Decrease in **SME** issuance
- **Re-emergence** of Leveraged Loan **CLOs**:
  - 2012: 0 deals
  - 2013: 19 deals YTD



**A very contrasted situation...**

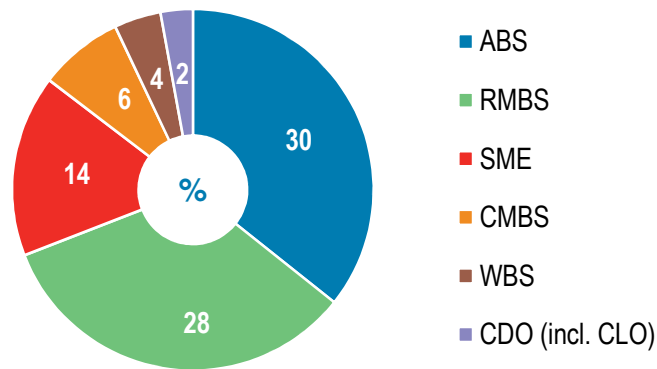


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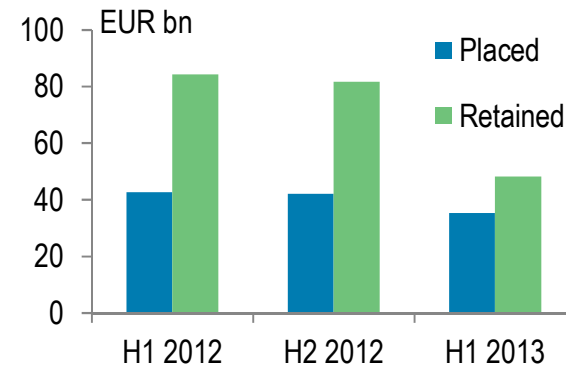
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# Zooming on 2013

## European primary issuance for H1 2013 by asset class

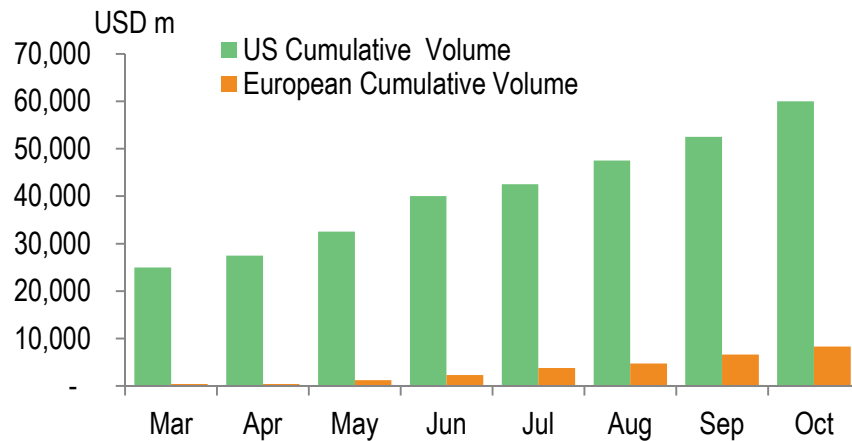


## European primary issuance by placement type



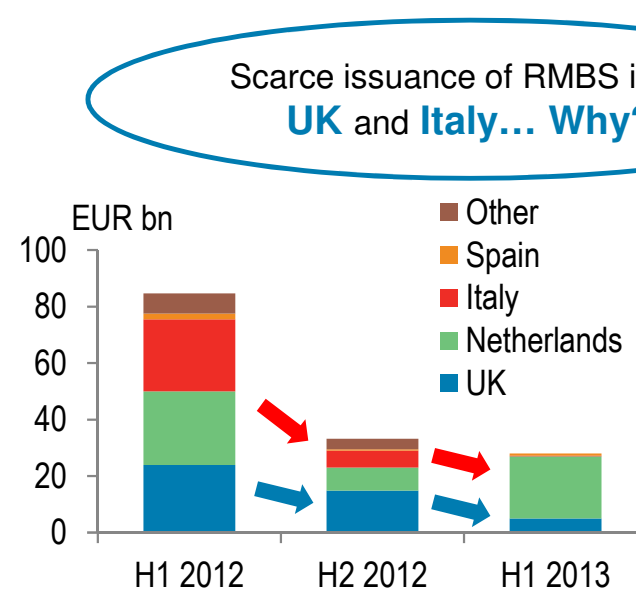
Decrease in retained deals: **> 40% Why?**

## Focus on CLOs: European vs. US 2013 cumulative issuance



US vs. European CLO issuance: **x10... Why?**

## Focus on RMBS: European issuance by country



Scarce issuance of RMBS in the **UK** and **Italy... Why?**



**A market that still presents signs of dislocation...**

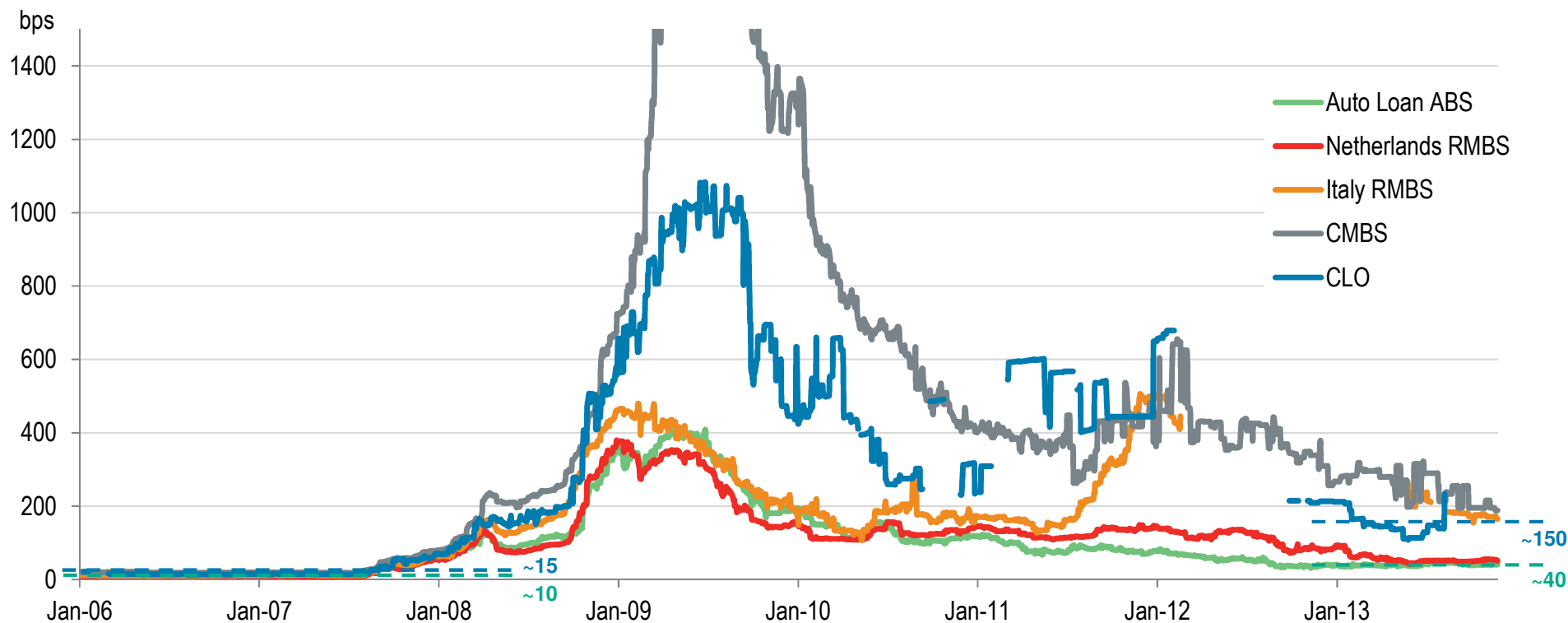


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# Secondary Securitisation Market Overview

Historical mid-spreads for selected European asset classes (original AAAs with WAL of 1-3yrs)

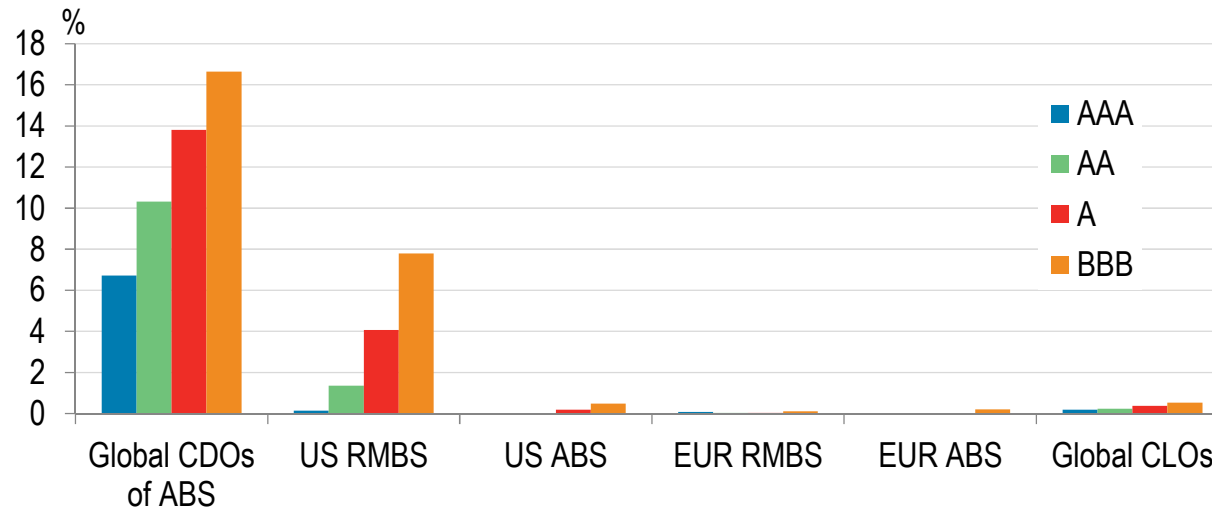


**Tightening over the last 2 years...**  
**...but a few asset classes still wide compared to 'prime' ABS**

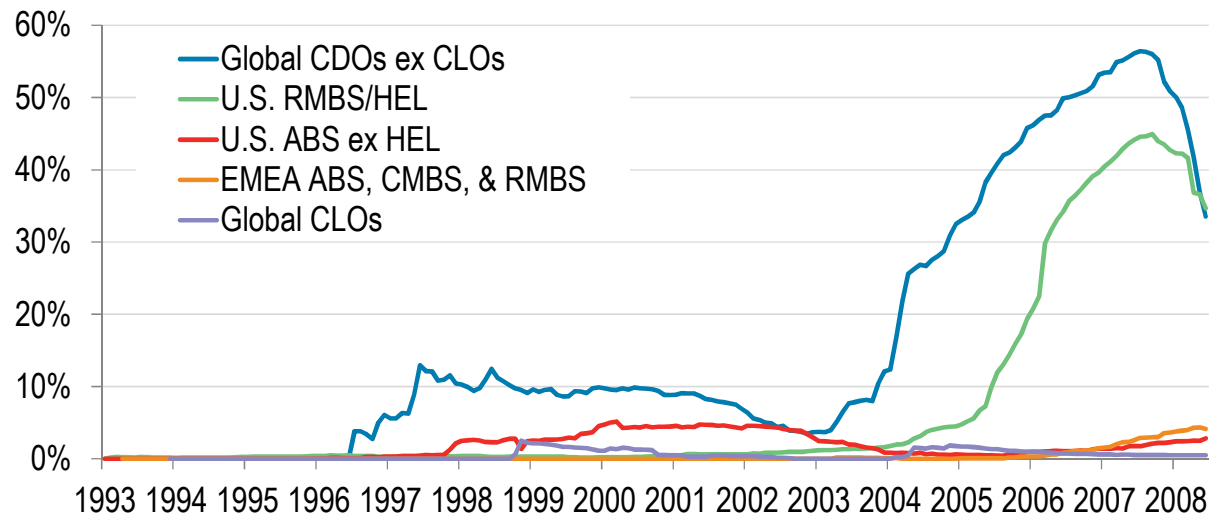


# Performance of Securitisation Transactions

## Structured finance average 1-year default rates (S&P, 1983-2012)



## Structured finance 5-year investment grade loss rates (Moody's, by cohort dates)



**Actual performance... better than assumed and misrepresented!**



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# Various Explanations...



## ■ To mention a few:

- **Macro factors:** growth, LT liquidity, sovereign, ...
- **Micro factors:** FLS, alternative funding, ...

## ■ One key factor... regulatory pressure:

### ➤ BCBS 236 – Revisions to the Basel Securitisation Framework (Capital Requirements):

- On December 2012, Basel committee published new proposals for securitisation capital requirements
- The proposals would result in **much higher capital requirements** for most securitisation positions including for high quality senior tranches
- Overly **conservative calibration**, with a **decrease in** the framework **risk sensitivity**

### ➤ Articles 404-410 of the Capital Requirements Regulation (“CRR”) (EU Risk Retention Rules):

- On June 2013, **CRR was formally adopted**, which replaces the CRD starting from 1 January 2014
- There remains great uncertainty with regard to the content and impact of the final version of the **RTS** due to be published shortly by the EBA
- Major impact on **CLO market**: retention by manager, definition of sponsor, MiFID registration...



...an uninterrupted deluge of regulations for banks, insurers and funds  
pushing towards greater disintermediation



# A Strong Dependence on Rating Agencies

## ➤ Regulation (EU) No 462/2013 (a.k.a. CRA 3):

- Requirement to solicit 2 ratings, with the intention of hiring at least one rating agency with small market share
- No guidance or technical standards yet

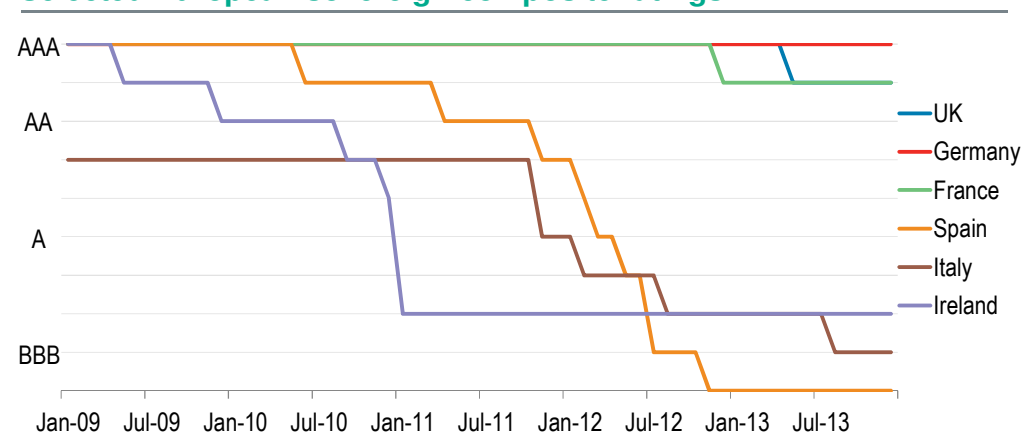
## ➤ Sovereign ratings caps continue to negatively affect bank funding:

- Continuing impact on ABS and covered bond ratings: new S&P proposal would penalise even more peripheral issuances
  - Spanish ABS capped at A?
  - Italian ABS capped at A+?
  - Portuguese ABS capped at BBB+?
- Additional country stresses in rating process
- Coupled to sovereign rating downgrades
  - ➔ Vicious circle on capital for investors

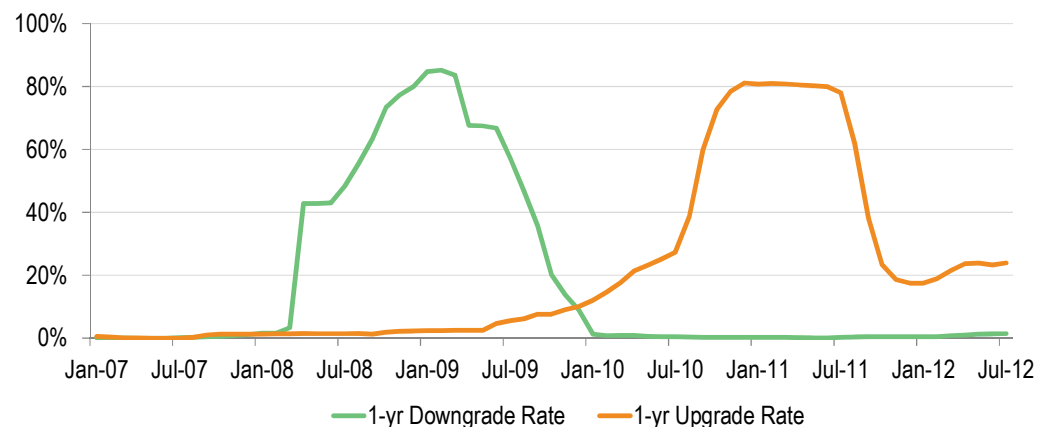
## ➤ Criteria updates with significant impact on the ratings of European transactions:

- Counterparty criteria updates  
e.g. S&P review of swap counterparties on RMBS
- Arbitrary stresses variations  
e.g. Moody's introducing in 2009 and then removing in 2011 severe PD stress for CLOs, resulting in rating swings

Selected European sovereign composite ratings



Moody's 1-yr downgrade and upgrade rates on global CLOs



# Challenges remain... Responses and Initiatives

## ➤ Industry responses to policy makers' proposals:

- BCBS 236 – Revisions to the Basel Securitisation Framework (Capital Requirements)
  - ➔ **Arbitrage-Free Approach**
- BCBS 245 – Recognising the cost of credit protection purchased (**synthetic securitisations**)
- Regulatory Technical Standards on **CRR retention rules**

## ➤ Focusing on funding the European economy:

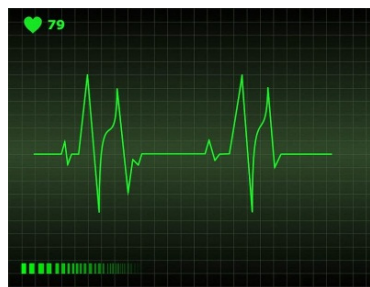
- EU initiatives on **SME lending**

*"You will hear more about supply-side initiatives, aimed for example at rebuilding securitisation and supporting SME lending, in coming months."* (Mark Carney, Oct 2013)

*"I see strengthening capital markets through securitisation as an important complement to bank lending. It bridges the financing needs of SMEs with the funds of non-bank investors."* (Yves Mersch, Nov 2013)

- A new step in the recovery process?
  - **From banks' life support...**  
(LTRO, Funding for Lending Scheme)

- **...to markets' vitamin boost?**  
(stronger capital markets, EIF-EIB framework on SME)



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