Association For Financial Markets in Europe

STS Framework – a securitisation plan for Europe?

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AFME – Members' Briefing Call
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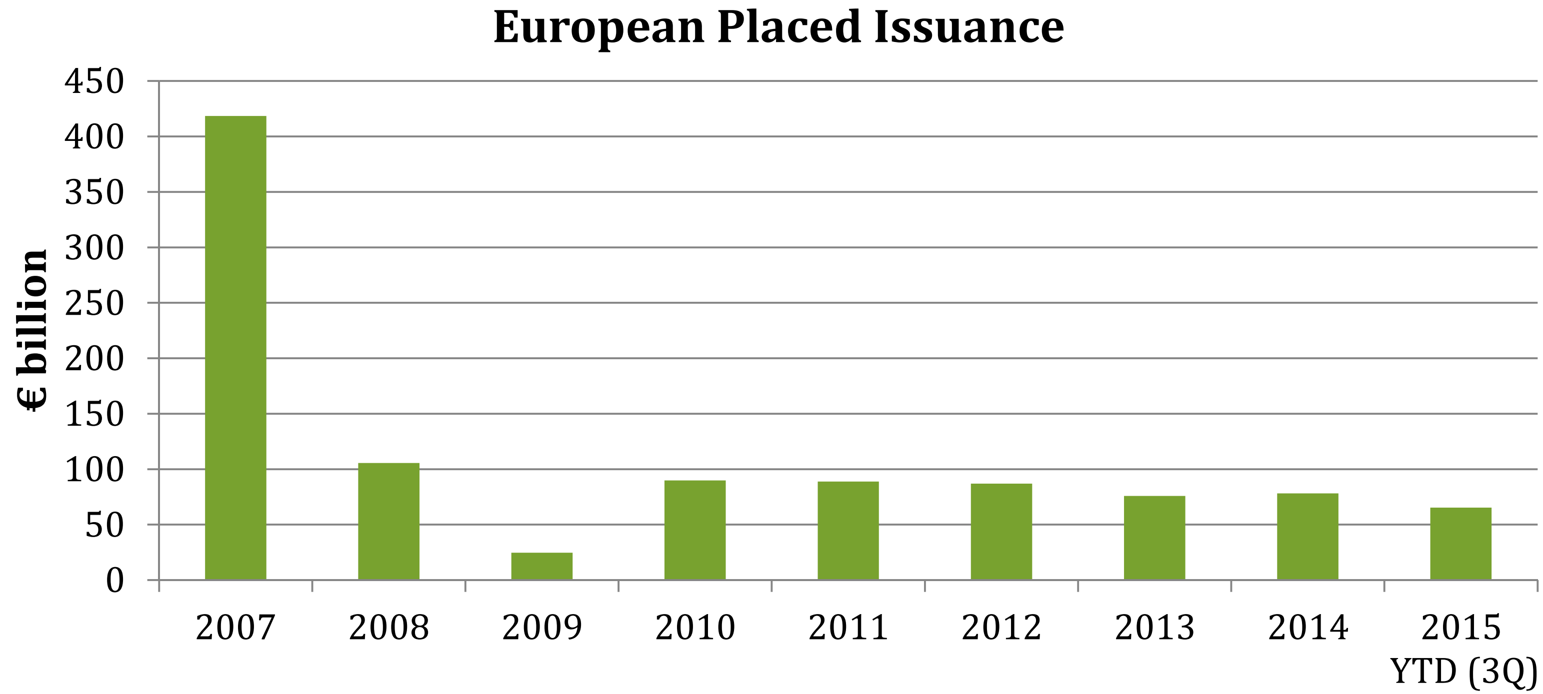
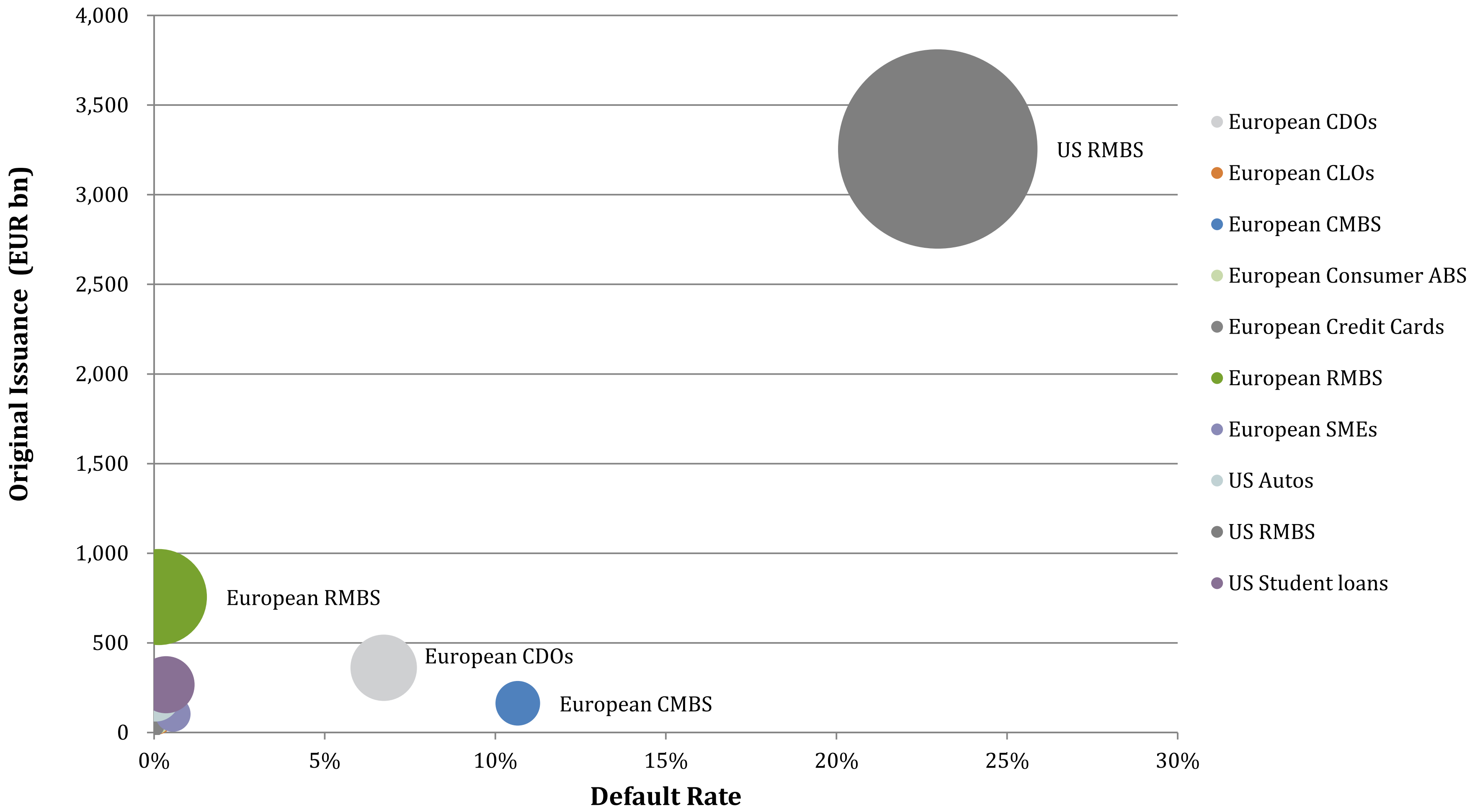
Placed European ABS primary issuance



Values in EUR bn	2007	2008	2009	2010	2011	2012	2013	2014	2015 YTD (3Q)
European placed	418.4	105.5	24.7	89.8	88.9	87.0	75.9	78.2	65.3
European retained	175.2	713.2	399.2	288.1	287.0	166.3	104.5	138.4	76.0
European retention (%)	30%	87%	94%	76%	76%	66%	58%	64%	54%
Total European	**593.6**	**818.7**	**423.8**	**377.9**	**375.9**	**253.2**	**180.5**	**216.5**	**141.3**
Total US	**2,080.5**	**934.9**	**1,385.3**	**1,203.7**	**1,056.6**	**1,579.2**	**1,515.1**	**1,131.5**	**1,240.0**

***Source**: AFME Q3 2015 Securitisation Snapshot*

Historical Default Rates for Securitisation: Mid-2007 to End Q2 2014



Source: Standard and Poor's

Historical Default Rates for Securitisation: Mid-2007 to End Q2 2014

	Original Issuance (EUR billion)	Default Rate (%)
Europe		
Total PCS eligible asset classes	**960.2**	**0.18**
Credit Cards	33.2	0.00
RMBS	756.0	0.14
Other consumer ABS	68.0	0.18
SMEs	103.0	0.55
Only senior tranches to be PCS labelled, the default rate for which is zero, like Covered Bonds		
Total Non-PCS eligible asset classes	**711.5**	**5.88**
Leveraged loan CLOs	70.6	0.10
Other ABS	68.8	0.00
Corporate Securitisations	47.9	0.17
Synthetic Corporate CDOs	254.4	2.88
CMBS	163.3	10.66
Other CDOs	77.8	6.54
CDOs of ABS	28.9	41.08
Total European securitisation issuances	**1,671.7**	**2.60**
Covered Bonds	**1,085.0**	**0.00**
Total European issuances	**2,756.7**	**1.58**
Select US asset classes		
Credit cards	295.4	0.14
Autos	198.2	0.04
Student loans	266.9	0.35
RMBS	3,254.9	22.97

Source: Standard and Poor's

The three components of the new securitisation framework

- A new Securitisation Regulation (SR) which will:
  - Set common core rules for all securitisations
  - Provide specific provisions for STS securitisations
  - Amend relevant sectoral laws: i.e. AIFMD, UCITS, CRA3, EMIR

- A comprehensive amendment of the Capital Requirements Regulation (CRR)
  - Revises prudential treatment of securitisations (in line with EBA's advice)
  - Implements the new Basel framework for general capital treatment of securtisation exposures

- Amendments to Solvency 2 and LCR will also be used to adjust existing calibrations and make other necessary revisions

- Next steps: parallel negotiations in the Council and the European Parliament

The Securitisation Regulation

- Defines the concept of Simple, Transparent and Standardised (STS) short and long term securitisation

- Aims to create consistency across a number of sectoral legislations (AIFMD, CRR, Solvency2)
  - Risk Retention
  - Regulatory Due Diligence
  - Transparency

- Applies to all securitisations and to all EU institutional investors investing in securitisation, to originators, original lenders, sponsors and SPVs

- Separate criteria for STS ABCP Securitisation

- Synthetic securitisations - out of scope at the moment

The new rules for risk retention

- Introduction of the a "direct" approach: EU originators, sponsor and original lenders under obligation to retain **minimum of 5 %** of net economic interests; investors still obliged to check if the retention requirements are met

- Article 4 SR - Exclusion of certain originators from being risk retention holders i.e. if it "has been established or operates for the sole purpose of securitising exposures"

- New RTS will specify retention requirements including the modalities of retaining risk, measurement of the level of retention, prohibition of hedging/selling the retained interest, retention on consolidated basis and exemption for indexes

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Regulatory due diligence broadly mirrors the existing CCR rules

- Article 5 SR requires that institutional investors "**verify** [if certain conditions have been met] before becoming exposed to a securitisation", including that:
  - The originator or original lender grants **all** its credits on the basis of sound and well-defined criteria
  - Originator, sponsor or original lender retains a material net economic interest and discloses it to institutional investors
  - Originator, sponsor and SSPE make available the information required by and in accordance with transparency requirement provisions

- Different procedures for **ongoing monitoring** are appropriate depending on whether the securitisation is held in the trading book or non-trading book

The new transparency rules intend to replace Art. 8b CRA

- The obligation to make information available to "holders of a securitisation position and to the competent authorities“:

  - Information on the exposures underlying the securitisation on a quarterly basis, or in case of ABCP, information on the underlying receivables on credit claims on a monthly basis.
  - Detailed description of the priority of payments of the securitisation ie. final offering document or prospectus with the closing transaction documents, asset sale agreement, assignment, derivatives and guarantees agreement.
  - Summary or overview of the main features of the securitisation (where prospectus is not available), including details regarding the structure of the deal, exposure characteristics, cash flow, voting rights of the holders of the securitisation position.

- ESMA to develop RTS on information and presentation of standardised template one year after entry into force of the Securitisation Regulation

General requirements for STS Securitisation

Simple (Art.8)	Sale or assignment Reps and warranties No active management	Homogeneity Ordinary course of origination and underwriting standards	No re -securitisation One payment No proceeds of sale
Transparent (Art. 10)	Historical data External verification	Cash flow model Loan –level data	Draft documents
Standard (Art.9)	Risk retention Hedging Standard rates	No reverse waterfalls Early amortisation Triggers to end the revolving period	Clear duties Default consequences Conflict resolution

Two tier approach for STS ABCP

Transaction Level	The remaining WAL of the assets may not exceed 2 years, and no underlying asset may have a residual maturity of more than 3 years.	The underlying exposures may not include residential or commercial mortgages.
Programme Level	The sponsor of the ABCP programme must be: a credit institution supervised under the CRD, a liquidity facility provider and must support all transactions in the ABCP programme. The sponsor must support all liquidity and credit risks and any material dilution risks of the securitised exposures as well as any other transaction costs and programme-wide costs.	None of the securities issued under the ABCP programme (which are required to predominantly consist of commercial paper with a final maturity of less than one year) may include call options, extension clauses or other clauses affecting the final maturity of the instrument.

- Problems remain in practical application: disclosures, private transactions, all underlying transactions must be securitisations

The calibration of CRR introduces the preferential treatment for STS Securitisation

- Implementation of the modular approach– the EC sets additional criteria under the CRR for STS securitisation by setting a cap on risk weights of underlying exposures (Art. 243)
  - 40% on weighted basis for Residential mortgages (weighted basis) + cannot contain loans with loan-to-value (LTV) ratio > 100%
  - 50% commercial mortgage (individual basis)
  - 75% retail exposure (individual basis)
  - 100% any other exposure

- The risk weight calculation under all risk weighting methodologies (SEC-IRBA, SEC-ERBA, SEC-SA) for positions in STS securitisation, with a risk floor lowered from 15% to 10% (for senior securitisations) (Art. 259 to Art. 264)

- Certain synthetic SME securitisations that are undertaken alongside public authorities can get STS treatment under certain conditions. (Article 270)

CRR - general framework for securitisation positions

- New hierarchy of approaches that are used to calculate securitisation risk weights (Art. 254):
  - Internal Ratings Based Approach (SEC- IRBA)
  - External Ratings Based Approach (SEC-ERBA)
  - Standardised approach (SEC-SA) (a fallback option)

- The look-through approach expanded to other senior securitisation positions (Art 267) – a maximum risk weight can be calculated on the basis of the capital charges associated with the underlying exposures

- The use of maximum capital requirements expanded to other methods than SEC-IRBA (Art 268)

- Stricter requirements for positions in resecuritisation (Art 269) – not only can resecuritisation not qualify for STS treatment, the proposal suggests further punitive requirements

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Our constructive engagement has been welcomed by all our interlocutors

- AFME's public position papers have been shared with the Commission and key national authorities.

- The most important issues include:
  - Sensible calibration of capital for bank and insurer investors: there are mixed views about whether the EC proposals are good enough to enable the market to revive
  - A revision of the LCR, and the relative treatment of ABS and covered bonds within that - the LCR is currently out of scope of the Commission proposals, this is seen by members as a dangerous omission
  - ABCP - the framework should work for the bulk of the ABCP market, not exclude nearly all of it (which it does right now)

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The EC proposals deliver strong start to the legislative process

- We welcome the recognition of the strong credit performance of European securitisation before, during and after the crisis

- The proposed adjustment to the Basel hierarchy enabling banks to use the Standard Approach where the External Ratings Based Approach produces a result "not commensurate to the credit risk", and other improvements to regulatory capital treatment

- Harmonisation of the current fragmented due diligence and risk retention regime across different investor types.

- Enabling investors to place "appropriate reliance" on the STS notification undertaken by originators, sponsors and SSPEs.

- Technical adjustments to some of the detailed STS criteria which broaden scope and incorporate existing prudent market practices

- However, further adjusment are needed and the time is of the essence

Q & A

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