
Press release

New report finds stringent aspects of EU Securitisation Regulation severely restrict growth of ABS investor base

14 June 2023

The Association for Financial Markets in Europe has today published a new report identifying the key challenges relating to compliance with investor due-diligence requirements under Article 5 of the Securitisation Regulation in the EU and UK and suggesting potential strategies to overcome such challenges.

The report finds that, under Article 5, investors are likely to interpret ambiguous provisions conservatively and in doing so will assume disproportionately high costs to the business. In addition, the report says that the regulation substantially reduces agility and flexibility in the investment process, thereby materially reducing investment opportunities for new investors, regardless of the credit risk, which in turn, impacts liquidity in the secondary markets and results in a less efficient market for all. These factors have the unintended effect of creating such high barriers to entry, even for seasoned credit investors, that it becomes challenging to build a business case to participate in the ABS market.

Shaun Baddeley, Managing Director of Securitisation at AFME, said: *“Revival of the securitisation markets relies upon targeted changes to various elements of the Securitisation Regulation and corresponding prudential frameworks. One crucial element with potentially material impact relates to regulatory obligations imposed on investors relating to due diligence. AFME has frequently referred to the lack of risk sensitivity embedded within specific areas of legislation. Article 5 that covers Investor Due Diligence is a good example of this.”*

Janet Oram, Head of ABS at USS IM said: *“The ABS market has made a huge effort to adopt the requirements of the securitisation regulations over the past few years. However, during this time it has become apparent that implementation has not been consistent between institutions due to differing interpretations of rules which is detrimental to the aim of a well-functioning market. Volumes have largely stagnated despite this being an important source of funding for the real economy and, as the world moves toward net zero, a perfect mechanism to finance some of that transition.”*

Marcus Mackenzie, partner at Freshfields said: *“While it is recognised that institutional investor due-diligence requirements play a central role in the modern securitisation market, the many uncertainties and different interpretations surrounding these undermine their very purpose of bolstering market confidence.”* Joana Fragata, senior associate at Freshfields added: *“Given that investor due-diligence requirements have been designed to allow institutional investors to properly assess the risks arising from all types of securitisations, having requirements that are flexible and driven by the actual needs of investors is vital for the proper functioning of the market and for unlocking the full potential of securitisation as a funding source for investment in the real economy.”*

To produce the report, AFME convened a working group composed of several non-bank investor covering different sectors of the market. AFME believes that the feedback gathered from the working group strongly suggests that there is a compelling case for reform in the interpretation of Article 5 of the Securitisation Regulation. This is also in line with industry feedback to the European Commission in September 2021, in response to the Commission’s targeted consultation on the functioning of the securitisation framework¹,

¹<https://www.afme.eu/Portals/0/DispatchFeaturedImages/COM%20AFME%20Response%20to%20Article%2046%20Consultation%2030%20Sept%202021%20Submission.pdf>

which confirmed that the Securitisation Regulation did not result in the widening of the investor base, given the significant barriers to entry. Therefore, reform will be key to unlocking the benefits of investor due-diligence and presents a renewed opportunity to attract investors back to securitisation and promote the growth of the sector.

The findings of this report precedes a second report that will follow later this summer, which will propose some guidance and clarifications in the form of Q&As, which could be used as a starting point by the relevant competent authorities in order to provide better clarity to market participants in the interpretation of such requirements. Ideally, this should be done by the relevant competent authorities via public guidance to create maximum transparency on the supervision of compliance.

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AFME (Association for Financial Markets in Europe) promotes fair, orderly, and efficient European wholesale capital markets and provides leadership in advancing the interests of all market participants. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) through the GFMA (Global Financial Markets Association). For more information, please visit the AFME website: www.afme.eu. Follow us on Twitter [@AFME_EU](https://twitter.com/AFME_EU)