



Setting the standard
for securitisation

T: +44 (0)20 3440 3720

E: info@pcsmarket.org

Prime Collateralised Securities
(PCS) UK Limited
40 Gracechurch Street
London EC3V 0BT

www.pcsmarket.org

Intervention by Ian Bell, Head of the PCS Secretariat to the European Parliament hearing on securitisation

I would like to thank the Rapporteur and the Committee for inviting me to speak today.

When we were set up as an independent not for profit initiative, the question we were tasked to answer was: “Is there such a thing as a safe securitisation and, if yes, what is it?”

It seems that the question is as important today as it was then.

Our intellectual journey started, as we believe it must, with the realisation of the destructive role played by some securitisations in the crisis that fell upon the world in 2007 and 2008. The role of US sub-primes and CDO cubes and their ilk in precipitating the financial crash requires us to ask what was it about these products that made them so damaging. Was it that securitisation itself was inherently flawed? Was it the assets that were securitised? How did this come to pass and how can we make sure that it does not happen again.

A detailed analysis of these disasters (as well as, by contrast, the extremely good record of most European – and, for that matter, Australian or Japanese – securitisations) indicates that it is not securitisation per se that is dangerous. The performance of these securitisation through the depth of the crisis shows that securitisation clearly can be done safely.

Our analysis, reflected in the work of public bodies such as the EBA, indicates that a number of separate and sometime cumulative failures underpin every single securitisation that collapsed in the crisis.

Each and everyone one contained one (or more) of four fatal flaws:

- the originate to distribute model where banks were encouraged not only to make worse and worse loans, with no skin in game, but to hide that fact;

- the abuse, way beyond their legitimate operational parameters, of mathematical credit models (in the re-securitisations);
- the reliance on market refinancing rather than borrower repayment were investors thought they held credit risk but in reality held much more dangerous market liquidity risk;
- the lack of transparency where some investors were sold securitisations of a level of complexity such that it was almost impossible to understand them.

Without such an understanding of the causes of the crisis, it is inconceivable that we should seek to proceed with any proposal to revive a securitisation market in Europe.

The question that poses itself to the Committee is whether the current STS proposal has learned these lessons and is therefore able (together with the considerable regulatory rules already written into law by the Parliament) to give us a sound basis from which to move forward in Europe.

We believe the proposal does contains specific provisions that address the fatal flaws identified from the crisis.

Does this mean the proposal can revive a European market? Some scepticism needs to be shown especially with regard to a number of areas where it falls short; one such area involves the need for proper market mechanisms allowing investors to invest safely.

We note the Rapporteurs' recent report focuses quite rightly on the need to ensure that investors take full responsibility for the fundamental credit analysis and understanding of their holding, avoiding a repeat of the overreliance on others for their core obligations. The report focuses also on the need for issuers to bear full responsibility for facts they disclose; we agree with both these approaches. But, investors have legitimately asked that common market mechanisms for certification be provided, under appropriate regulatory supervision, to assist them with the compliance process – a process distinct from the credit analysis process which they must “own”; a mechanism similar to the way auditors or consolidated tape providers in MIFID provide them with the basis on which they are able to start their process of analysis. They will also welcome the Rapporteur's call for a single European point of interpretation for what must be a single European market and the idea of data repositories for necessary information.

I would be happy to elaborate on any of these aspects should the Committee feel this might be valuable.

13th June 2016