PCS 2023 DUBLIN SYMPOSIUM

SECURITISATION

AN INDISPENSABLE TOOL FOR GROWTH AND CAPITAL MANAGEMENT

DUBLIN 17 JANUARY 2023

IN ASSOCIATION WITH

A&L Goodbody KBRA

Opening Remarks

Ian Bell

CEO

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Gordon Kerr

Managing Director

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Presentation

Securitisation: Introduction to the European Securitisation Market Part 1: History

Ian Bell

CEO

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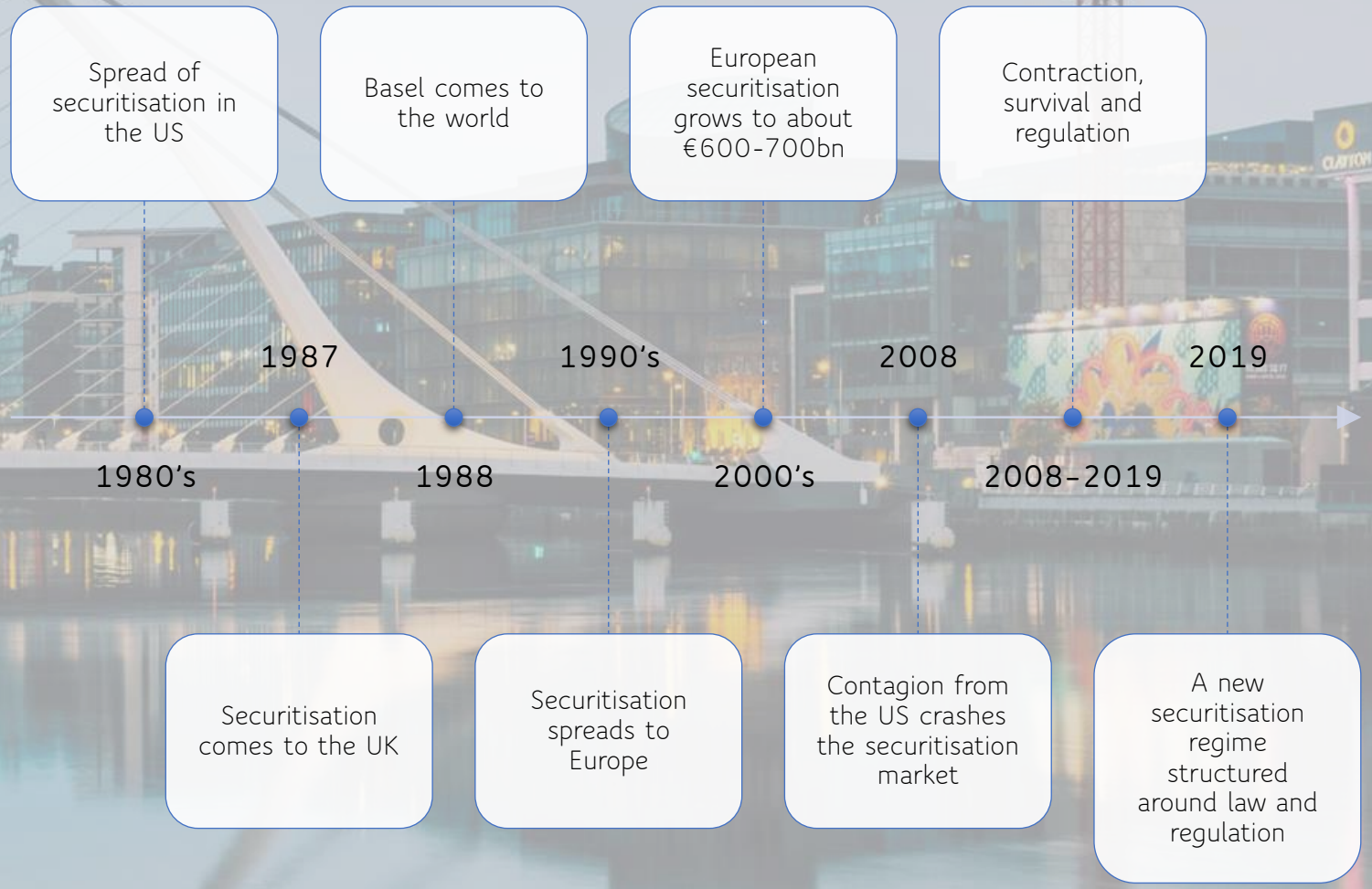
Securitisation Short History

Milestones..



Securitisation Short History

80's – "Its not about size"

- 1980's ROE and ROA eclipses Asset Size in bank rankings
- This change drives "securitisation" because….
- Capital follows accountancy and accountancy allows the deconsolidation of "securitised" assets
- So excess spread gives you infinite returns making securitisation **the trend** of the 80s in the US

Securitisation Short History

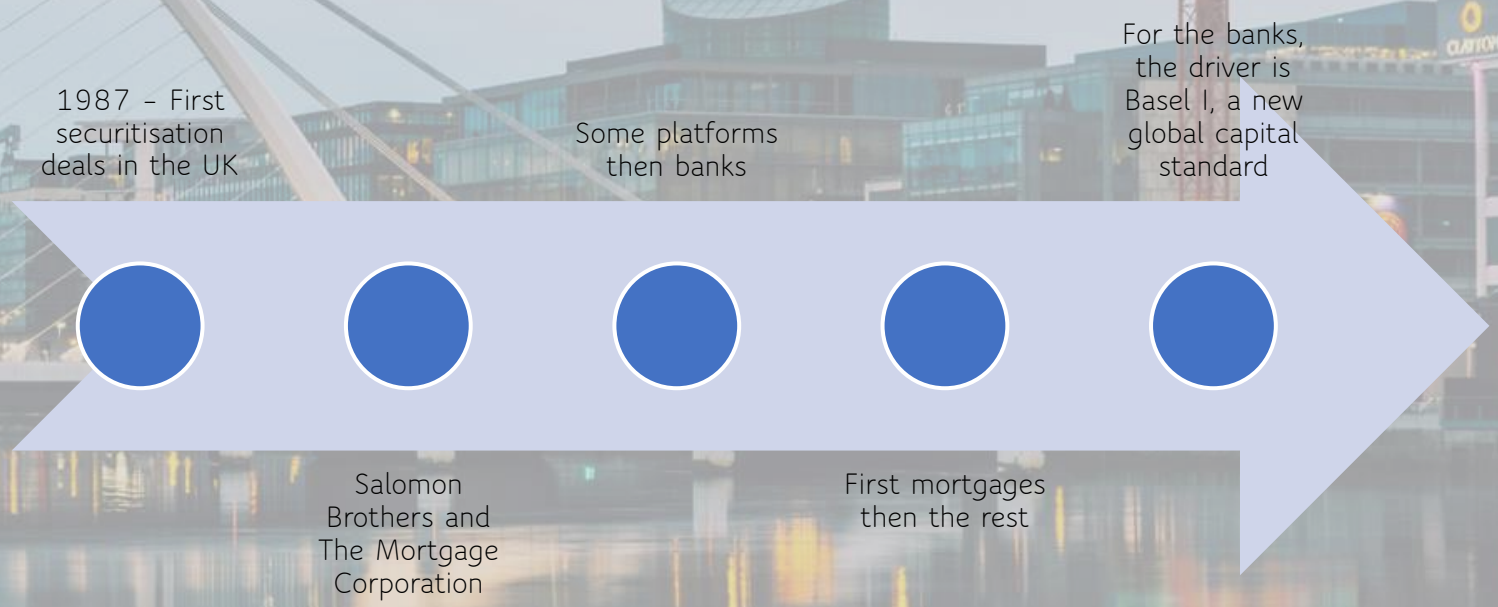
Europe

Securitisation is the cutting edge but still seen as suspiciously American in the 90's but spreads at different speeds through Europe

Note: transactions were done, eg in Italy before the law was passed

Securitisation Short History

The UK



Securitisation Short History

European Growth

From the 90's to 2007/2008 securitisation grows across Europe

We have seen transactions in the following asset classes:

- Residential mortgages
- Commercial mortgages
- SMEs
- Auto Loans
- Auto Leases
- Credit cards
- Consumer loans
- Broadcasting entitlements of soccer
- Corporate Loans
- Equipment Leases
- Shipping Loans
- Aircraft Loans
- Non-performing Loans
- Whole Businesses and
- …movies, diamonds and champagne

Securitisation Short History

European Growth

European countries with securitisation issuance before the GFC

- Austria
- Belgium
- Finland
- France
- Germany
- Greece
- Ireland
- Italy
- Portugal
- Russia
- Spain
- Sweden
- Switzerland
- The Netherlands
- United Kingdom

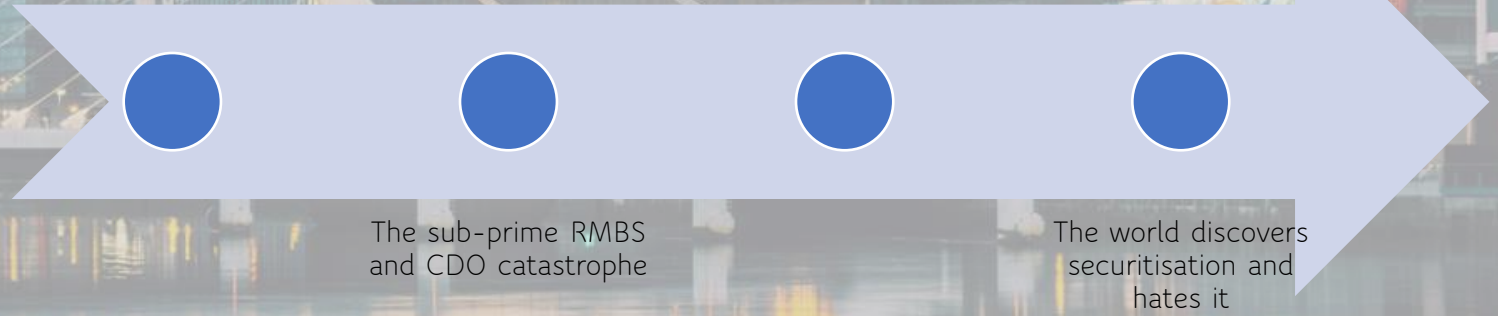
Securitisation Short History

World Growth

Countries outside Europe with meaningful securitisation markets then and today

- Canada
- Mexico
- South Africa
- Russia
- Japan
- China
- Australia
- New Zealand

Securitisation Short History



After the rise, the fall

Securitisation Short History

Lessons from the crisis

Outside of CMBS and CDOs, **losses on senior tranches (AAA to A) of European securitisations were literally zero**

As the crisis unfolded it became clear that the **problems of US securitisations had not been replicated in Europe** (save for CDO's)

Issues with securitisations:

- Disclosure issues – too little sometimes, too much often
- Originate to distribute model
- Re-securitisation – models on models
- Re-financing – from credit to liquidity risk

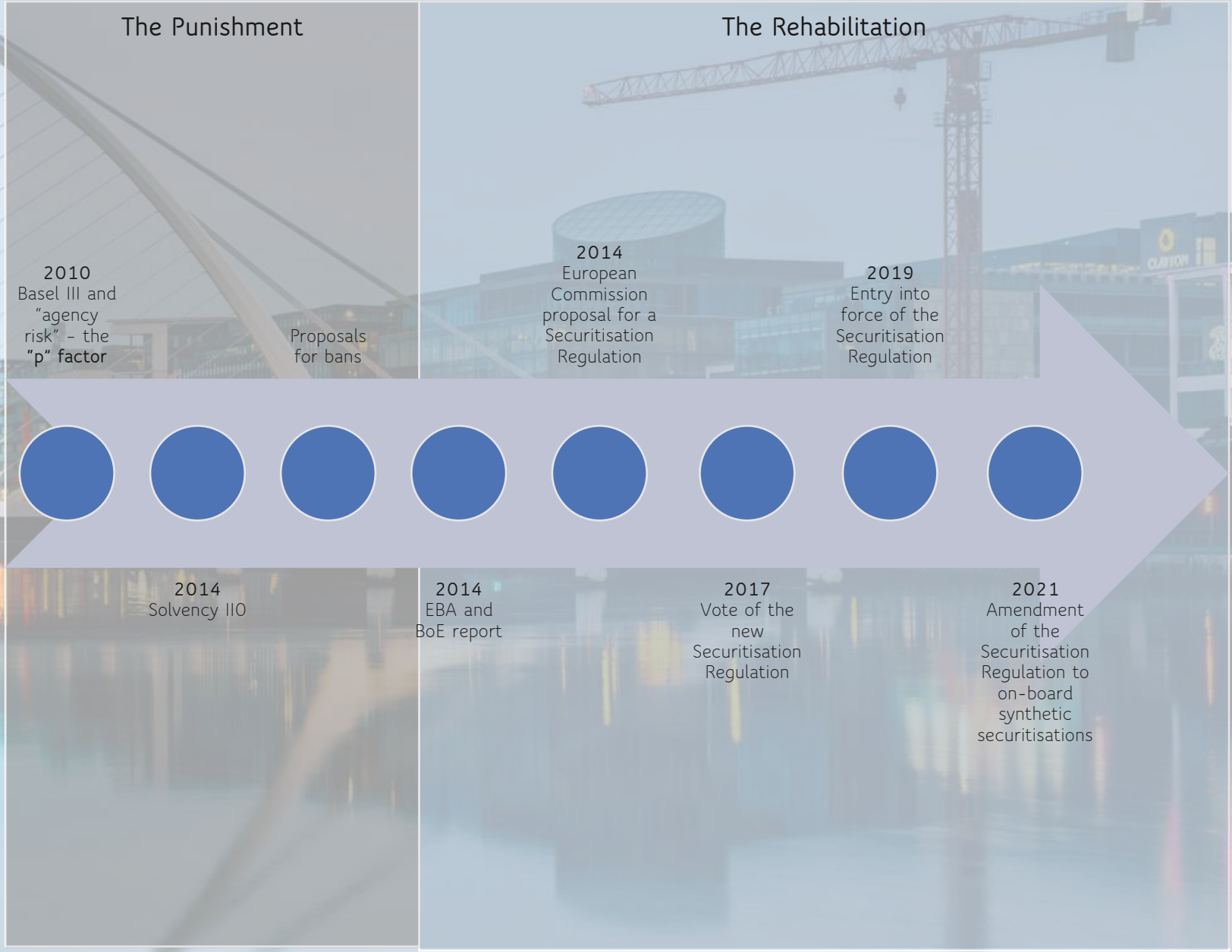
Securitisation Short History

After the fall, the rehabilitation

	Original Issuance (EUR billions)	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	65.0	0.16
SMEs	106.0	0.56
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	5.85
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	10.56
Other CDOs	77.8	6.54
CDOs of ABS	28.9	41.08
Total European securitisation Issuance	1571.7	2.60
Covered Bonds	1385.0	0.00
Total European Issuances	2756.7	1.56
Select US asset classes		
Credit Cards	296.4	0.14
Autos	196.2	0.04
Student loans	266.8	0.35
RMBS	3254.9	22.97
Stats for issuance before the GFC		

Securitisation Short History

From fall to rehabilitation



Presentation

Securitisation: Introduction to the European Securitisation Market Part 2: Foundation

Ian Bell

CEO

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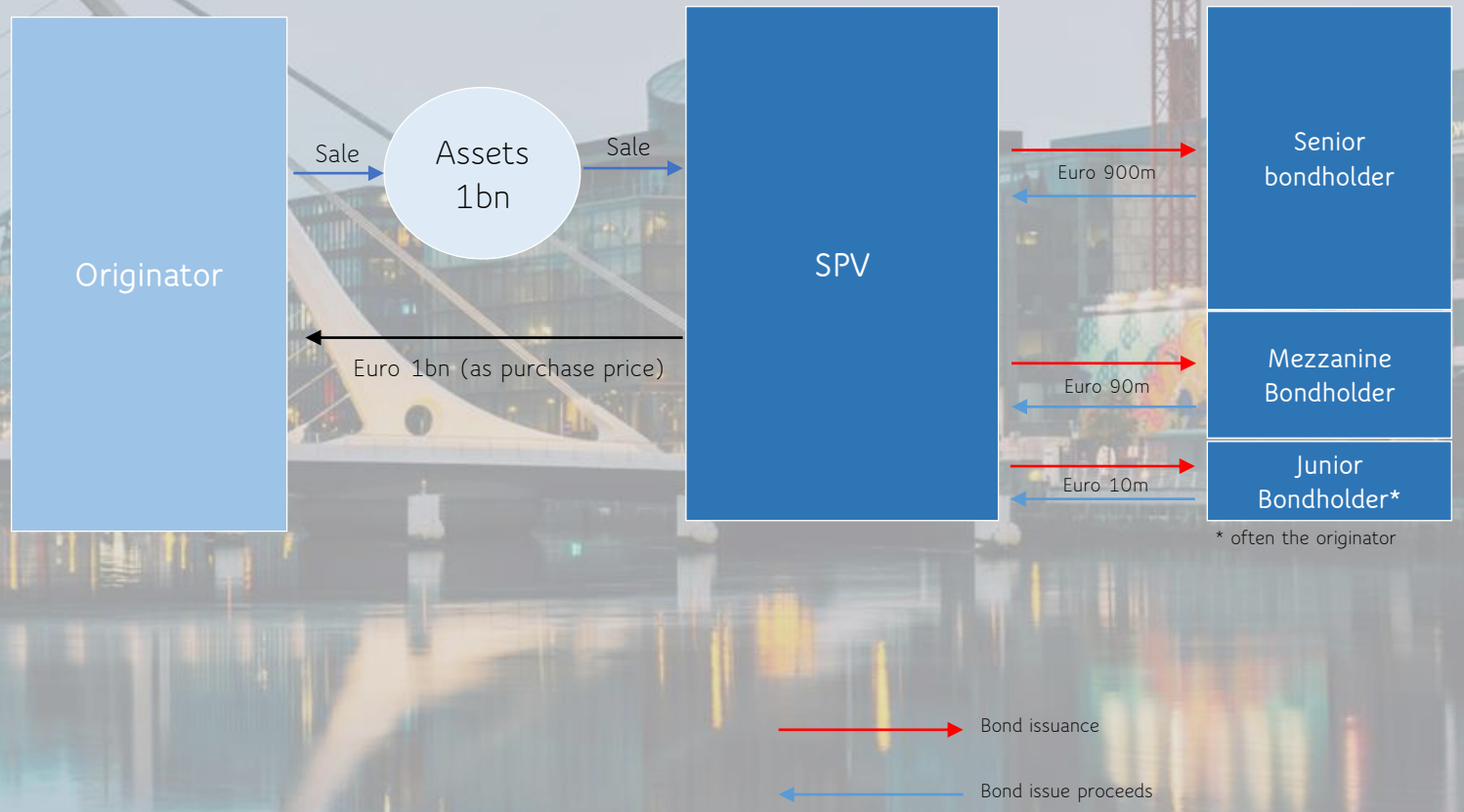
Securitisation Key Concepts

Tranching
The Classic



Securitisation Key Concepts

The heart of all securitisations lies in two key concepts:

Asset-only risk

Tranching

What is all about

Securitisation Key Concepts

Asset-only risk

- Securitisation is NOT secured finance
- A securitisation investor ONLY takes the risk of the securitised assets
- If the assets perform, the securitisation investor is paid back
- If the assets do not perform, the securitisation investor suffers those losses
- For a financing to be a securitisation, the two points above must be met EVEN if the bank that originated the assets has defaulted, is insolvent or even is liquidated

Securitisation Key Concepts

Pass-through & match funding

Securitisation being an asset-only risk leads necessarily to another key aspect of securitisations: **"pass-through"**

Pass-through means that the investors in a securitisation can only look at the asset to be repaid (asset-only risk), not the ***originator***

Pass-through means that the investor only gets paid when the securitised asset pays. In some cases (e.g., mortgages and credit cards) this is unpredictable

For the ***originator*** *that means that funding is matching the repayment profile of the assets.* ***No funding miss-match****. This is known as "****match-funding****"*

So, in securitisations usually, the **investor** does **NOT** have a bullet repayment at maturity and may not know exactly when he is going to get paid

Securitisation Key Concepts

True sale

Securitisation being an asset-only risk leads necessarily to another key aspect of traditional securitisations: "true sale"

"true sale" means that the investors in a securitisation get repaid even if the originator goes bankrupt

If the securitised assets were only security, all jurisdictions have rules suspending the enforcement of security. This would mean that, in the bankruptcy of the originator, securitisation investors may not be able to get their hands on the securitised assets and so would be dependent in some way on the originator to get repaid

So, to be an asset-only risk, the securitised assets are sold by the originator in a "true sale" that will be recognised by the courts even if the originator is bankrupt

Securitisation Key Concepts

Asset-only risk & true sale give you

The **SPV**

"True sale" requires the securitised assets to be sold by the originator to avoid being trapped in the originator's bankruptcy

But where do you put the assets now you have sold them? Who is buying them?

The ***special purpose vehicle (SPV)*** is a corporate entity set up just for the securitisation and has the following characteristics:

No employees	No other activities	Tax neutral	Independent

This makes it ***insolvency remote***

Securitisation Key Concepts

Tranching

Securitisations are "*tranched*": the risk of the securitised assets is divided in horizontal slices

The assets securitised are *pools* of multiple single financial assets

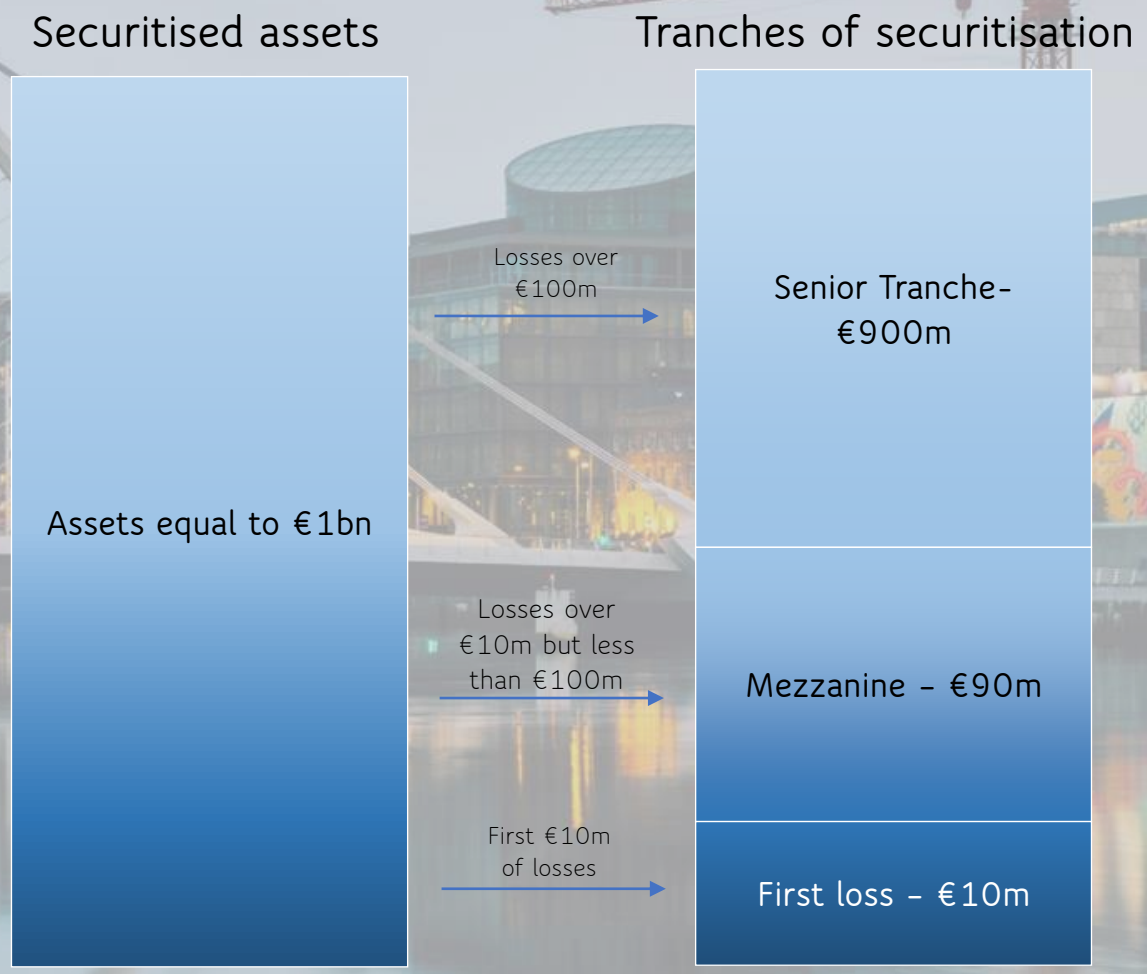
Tranching means that the financing of the pool of assets is made up of different debt instruments ranked by seniority.

The way they are ranked by seniority is that, if defaults happen to the underlying securitised pool, the investors in the lowest ranked debt absorb those losses first, until they are wiped out. Then losses are absorbed by the next highest "tranche" of debt

Securitisation Key Concepts

Tranching

It's easier with a picture



Securitisation Key Concepts

Tranching

In the example, the investor in the senior tranche will not lose money unless more than 10% of the underlying assets have defaulted

A credit analysis of the underlying pool will tell the investor how likely or unlikely a 10% loss would be

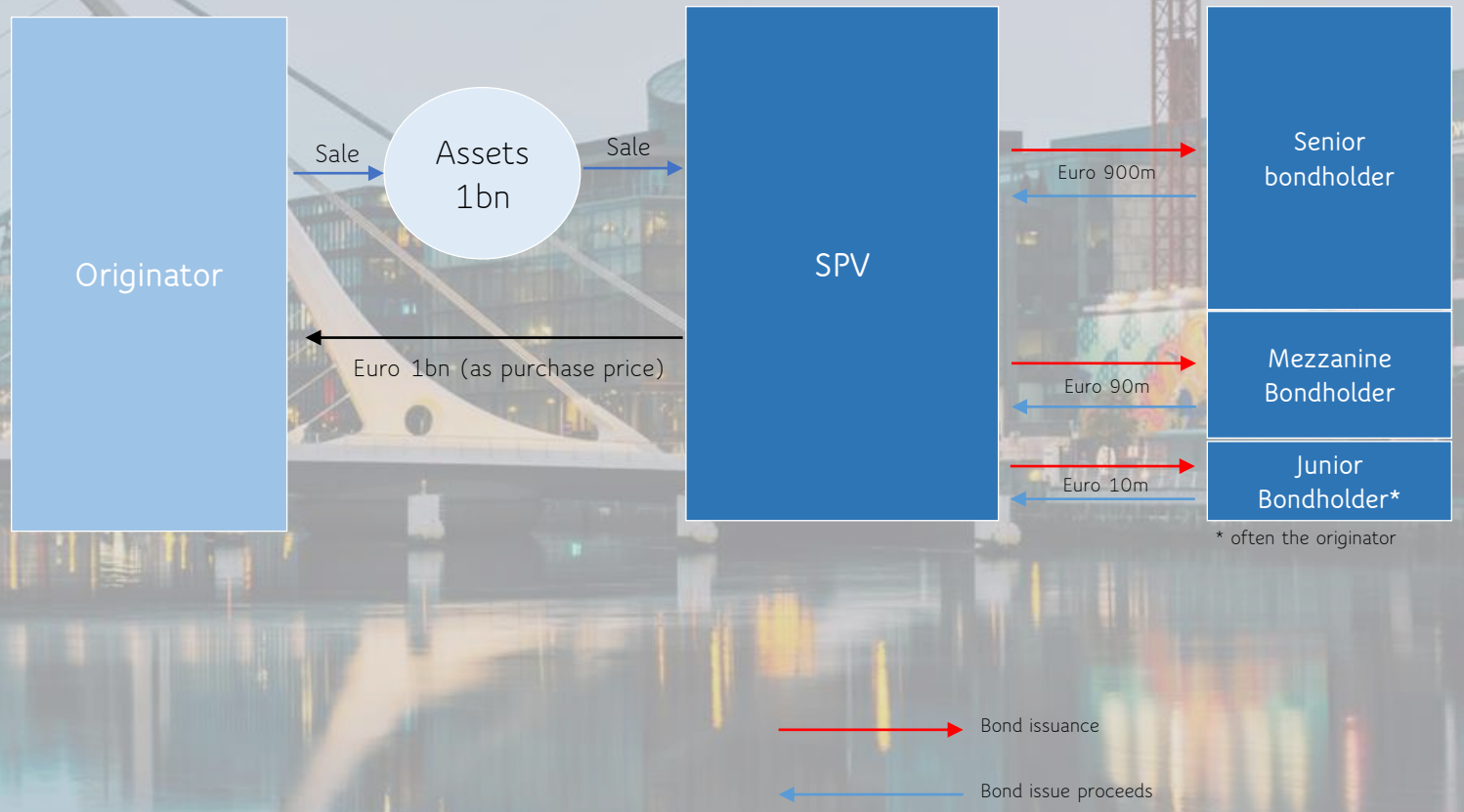
If a 10% loss is extremely unlikely, the senior tranche is extremely safe and so the senior investor will accept a low return (interest rate) to reflect the safety of the tranche

So, another **securitisation rule**:

"the lower the tranche in the stack, the higher the risk and so the higher the interest rate"

Securitisation Key Concepts

Tranching
The Classic



Securitisation Key Concepts

Despite how it is sometimes presented, **securitisation is not alchemy**

Securitisation **cannot turn lead into gold** or low credit risk into high credit risk

The **total risk of a pool** of securitised assets **remains the same**

If you add the credit risks borne by the senior bondholder, the mezzanine bondholder and the junior bondholder, it sums to the exact same credit risk of the pool

But if you think of the pool as a mixed lot, securitisation **can separate the gold** in the pool **from the lead** in the pool

Tranching WARNING!

Securitisation Key Concepts

The Waterfall

- As cash is generated from the securitised assets and received by the SPV, it is distributed in a specific order. That order is the "waterfall"
- The archetypal waterfall looks somewhat like this:
  - Entities that have to be paid if the securitisation is to continue (servicing fees, swap fees, admin expenses….)
  - Liquidity fees
  - Swap payments
  - Most senior noteholders
  - Mezz noteholders
  - Junior noteholders
  - Excess spread to the originator
- This is an idealised list and waterfalls can be quite complex
- There are usually two waterfall – interest and principal
- There can also be two waterfall – pre and post enforcement

Securitisation Key Concepts

Liquidity

- The cash flow from the assets may suffer for irregularities over time when the securitisation bond must pay in accordance with its schedule eg consumers paying late
- To prevent asset cash flow irregularities resulting in the technical default of the securitisation bond, a bank may provide a committed loan facility to the SPV to be drawn on in case of a cash shortfall. This loan is a "liquidity facility"
- Because the liquidity facility is liquidity not credit support, it gets repaid before the securitisation notes in the waterfall

Securitisation Key Concepts

The Servicer

- The SPVS is insolvency remote so has no employees
- Someone has to service the assets – collect cash, send chasing letters, enforce defaulted receivables
- The "servicer" is usually the originator but not always
- Sometimes a party is appointed upfront in case the servicer is not capable of acting – this is called a "back-up servicer"

Securitisation Key Concepts

Warehouse Facility

- There is a minimum size for a securitisation placed in the public markets
- So how does a non-bank finance the original lending to create the assets that will go in the securitisation pool?
- One financing tool is a committed loan facility from a bank which is itself a securitisation (ie asset backed and tranched). These are called "warehouse facilities" or just "warehouses"
- A customer borrows from the originator eg for example a house purchase. The originator draws down on the committed loan facility in the amount of the mortgage and advances the funds.
- There is an agreement between the lending bank and the originator that when a certain amount of origination has been reached, the originator will refinance the pool via a securitisation
- Because warehouses are legally securitisations, they must comply with the Securitisation Regulation
- The capital that must be allocated by the lending bank is the CRR required capital for a securitisation
- But that means that warehouses can also achieve STS status and a lower capital allocation as a result

Securitisation

Why do it if you are an originator?

Asset-only means securitisation is a form of **financing** ***accessible*** *even when the bank is weak or in danger*

Asset-only means that for a weak bank with strong assets, the ***cost of financing can be lower***

Tranching means that the bank using securitisation can **access** ***new investors*** that would not finance it on an unsecured basis

Tranching means that, by targeting specific investor groups and appealing to their specific risk/reward targets, *the* ***total cost of funding may be lower*** than without tranching

If the **investors take the asset risks**, it means that those risks are **not borne by the originator** and therefore **no capital need be set aside against those assets** – securitisation can be *a* ***capital management tool***

Securitisation

Why do it if you are an investor?

Tranching means that securitisation can create **high quality capital market debt** from mixed quality assets for risk averse investors seeking a good return

Asset-only finance means that capital market **investors can lend** (indirectly) and take the risks of **markets to which they have no other access** (e.g., SMEs or residential mortgages)

The European nature of the market means **investors** can have **access to safe capital market instruments in jurisdictions** to which they have **no other access**

Because **rating agencies allow senior tranches** of securitisations to be **rated higher than the sovereign**, securitisation allows low risk investors to invest in high-risk countries

STS Regime

A&L Goodbody KBRA RCS

STS Regime

Origins

2007-2008
- Financial crisis engulfs the world
- Securitisation is considered a key culprit

2008-2009
- Tsunami of new financial regulations across the world
- Securitisation "punished" (Basel 2 changes, Solvency II, etc.)

2009-2011
- Financial crisis becomes a sovereign crisis – EU deeply concerned about the future of European finance
- But EU securitisations weather the crisis extremely well - public authorities start to wonder (ECB, BoE, EC….)

2012-2014
- "Good securitisation" becomes rehabilitated in policy circles
- Official sector looks to soften the regulatory punishment but only for "high quality" securitisations

2015
- EBA Report and European Commission legislative proposal
- A new definition of high-quality securitisation is proposed: STS

2017-2019
- Law is passed in December 2017
- Law comes into force on 1st January 2019

2021
- Law is amended to include synthetic securitisations and to fix some issues with NPLs

STS Regime

THE LAW

(EU) 2017/2402

General framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation **("STS Regulation")**

amended by

(EU) 2021/557 - amending Regulation (EU) 2017/2402 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation to help the recovery from the COVID-19 crisis **("Synthetic STS Regulation")**

STS Regime

THE LAW Structure

- The "STS Regulation" is also called, probably more accurately, the "Securitisation Regulation" as it sets out the rules for all securitisations in the European Union
- The STS Regulation is therefore two sets of rules in one legislative text
- The first part of the Regulation (articles 5 to 17) sets out the rules applicable to all securitisations and market participants
- The second part (articles 18 to 28), sets out the rules for the STS regime
- The third part (articles 29 to 48) is concerned with procedural and regulatory matters (including the respective powers of various regulatory bodies and sanctions)
- *Note: the new 2021 regulation allowing synthetic STS transactions amended this regulation but left the structure broadly unchanged*

STS Regime

Securitisation Regulation

Obligations relating to:

- due diligence
- risk retention
- disclosure
- credit-granting standards
- ban on resecuritisation

STS - "simple, transparent and standardised"

Has applied from 1 January 2019 to:

- New securitisations
- Transactions with a new issuance of securities or creation of new securitisation positions

STS Regime

Securitisation Regulation

Definition of "securitisation":

- a transaction or scheme where the credit risk of an exposure or pool of exposures is tranched
- payments are dependent on the performance of the exposure/pool of exposures
- subordination of tranches determines the distribution of losses throughout the life of the deal (not just on default)

Definition of "tranche":

- a contractually established segment of the credit risk associated with an exposure or a pool of exposures
- a position in the segment entails a risk of credit loss greater than or less than a position of the same amount in another segment, without taking account of credit protection provided by third parties directly to the holders of positions in the segment or in other segments;

STS Regime

Securitisation
Regulation
Due Diligence

"institutional investor" needs to do the following:

- verify :
  - credit-granting based on sound and well-defined criteria and clearly established processes;
  - compliance with risk retention;
  - originator, sponsor or SPV has, where applicable, made available information as required by Article 7 (transparency)
- assess risk characteristics, structural features and, if applicable, compliance with STS requirements
- monitoring, stress tests, internal reporting, be able to demonstrate understanding of the securitisation position, risk management procedures

STS Regime

Securitisation Regulation Disclosure

- "Public" deals (securities listed on an EU regulated market):
  - Disclosure to a securitisation repository
- "Private" deals:
  - Disclosure to be made available to investors, potential investors (upon request), and to competent authorities
  - Local law notifications to competent authorities
- Designation of reporting entity
- ESAs' opinion/report
- Technical standards now in force – specify information and reporting templates for non-ABCP (by asset class) and ABCP

STS Regime

Overview

ORIGINATOR/SPONSOR/SSPE*

SECURITISATION

notification

Third party verification

ESMA

WEBSITE

EU-REGULATED INVESTORS

Better regulatory treatment

STS CRITERIA*

SIMPLICITY	TRANSPARENCY	STANDARDISATION
✓	✓	✓

**Must be in EU to be capable of being STS*

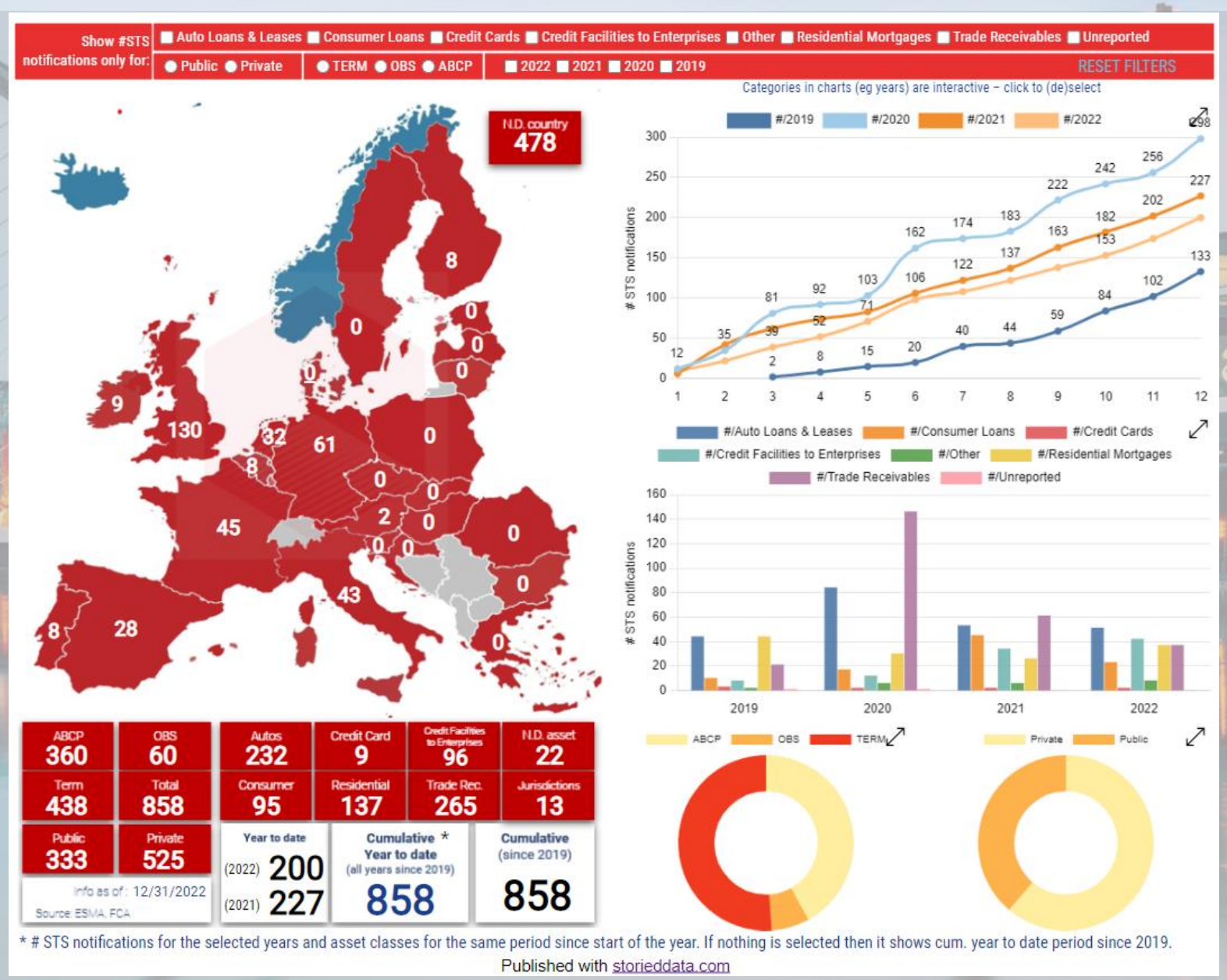
STS Regime

THE LAW
Benefits of STS

- The CRR Regulation provides for lower capital requirements for EU bank investors holding STS securitisations that also meet some additional requirements
- The Money Market Funds Regulation provides that money market funds can only invest 10% of their holding in securitisations. This limit is increased to 15% for STS securitisations
- The Solvency 2 legislation provides for EU insurance companies to hold substantially less capital against the senior tranches of STS securitisations
- An amendment to the Liquidity Cover Ratio ("LCR") rules changed the eligibility rules for LCR to the benefit of STS

STS Regime

Issuance so far..




Coffee Break
A&L Goodbody
KBRA

Presentation

Macro effects and securitisation

Alexander Batchvarov
Managing Director
Bank of America

A&L Goodbody KBRA

Presentation

Securitisation : An indispensable tool for growth and capital management

Harry Noutsos
Managing Director
PCS

A&L Goodbody KBRA PCS

Significant Risk Transfer

What can an SRT transaction do for you?

Increase Capital Velocity

Improves ROE & NII

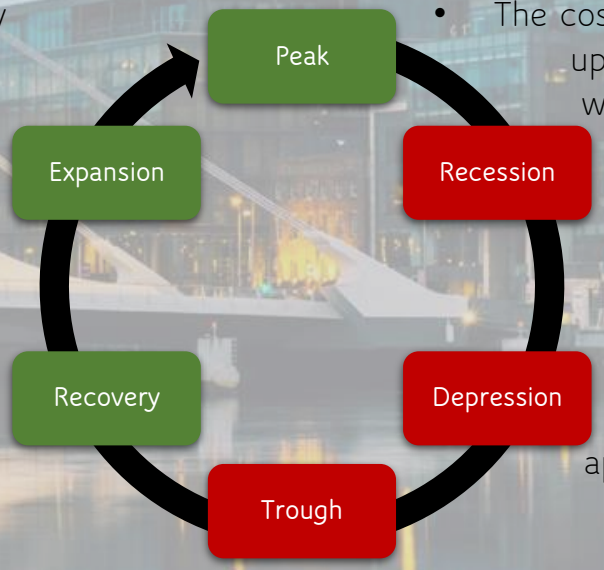
- Capital relief can improve ROE and NII via origination of new assets without the need for more capital
- Enables the bank to benefit from growing economic activity
- Cost is stable through the lifetime of the transaction

Risk Sharing

- The risk of the portfolio is shared with non-bank investors
- Acts as a check on the business origination
- Cheaper funding via lower average RWA

Concentration management

- Allows the reduction of concentration limits
- Allows the continuation of origination of loans in industries with high concentration limits



Capital Protection during a downturn

Insurance against a downturn

- Protects the bank's profitability and capital against an economic downturn
- Allows for the continuation of loan origination
- The cost of the insurance is known upfront and does not increase with the worsening economic conditions

When do buy Insurance

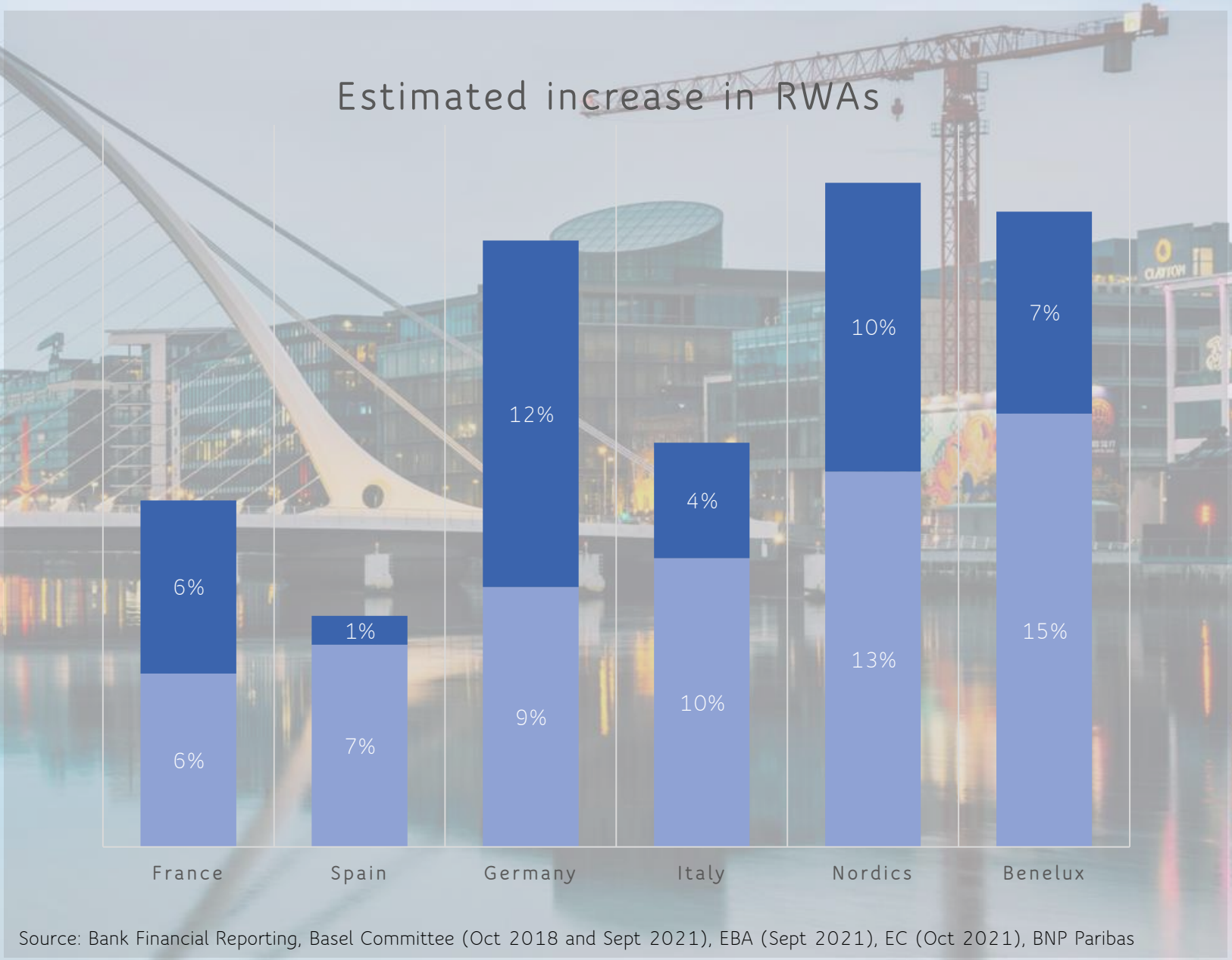
- The best time to buy insurance is when you don't need it
- In a downturn the market appetite is low and expensive

Can I buy Insurance

- In order to benefit from the SRT investor base the bank needs to have the right infrastructure in place
- Typically, it can take between 1-2 years for the infrastructure to be put in place

Synthetic SRT

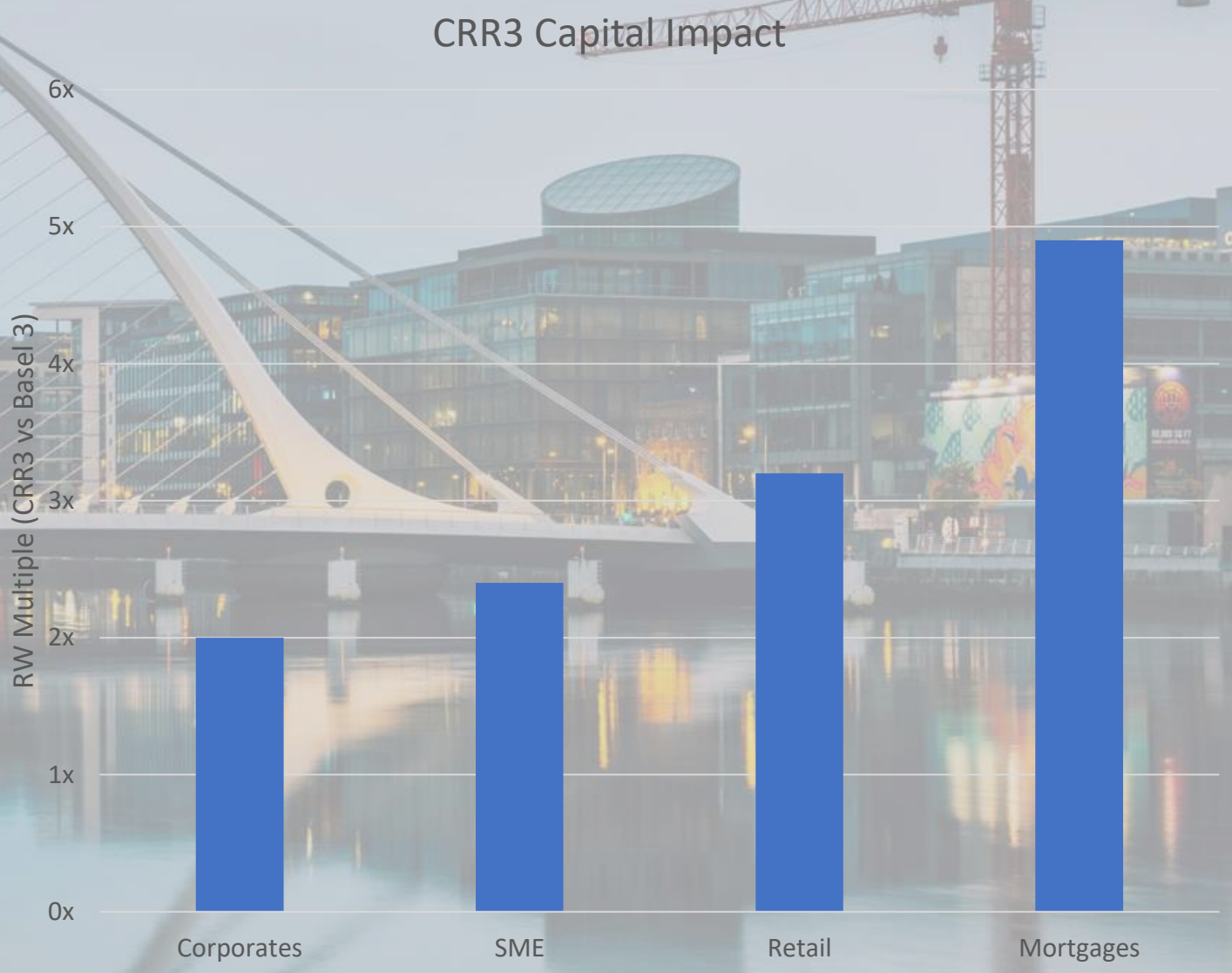
What can an SRT transaction do for you?



Source: Bank Financial Reporting, Basel Committee (Oct 2018 and Sept 2021), EBA (Sept 2021), EC (Oct 2021), BNP Paribas

Synthetic SRT

What can an SRT transaction do for you?



Source: Bank Financial Reporting, Basel Committee (Oct 2018 and Sept 2021), EBA (Sept 2021), EC (Oct 2021), BNP Paribas


Lunch
A&L Goodbody
KBRA

Panel Discussion

SRT – Growth in the use of synthetic securitisation – replacement of traditional ABS?

Moderator

Harry Noutsos

Managing Director

PCS

Sinead O'Connor

Partner

A&L Goodbody

AnneMarie Flynn O' Reilly

Head of Structured Investments

AIB

Alan McNamara

Managing Director

Bank of Ireland

Gordon Kerr

Managing Director

KBRA

A&L Goodbody KBRA PCS

Firechat

Developments in the Solar & Green Finance Market

David McElroy

Partner

A&L Goodbody

Killian Walsh

Senior Director

KBRA

A&L Goodbody KBRA


Coffee Break
A&L Goodbody
KBRA

Panel Discussion

Development of Irish Market

Moderator

Peter Walker

Partner

A&L Goodbody

Glynis Webb

Structured Investments

AIB

Marie Gaffney

Head of Treasury

Dilosk

Boudewijn Dierick

Managing Director

Auxmoney

Gordon Kerr

Managing Director

KBRA

A&L Goodbody KBRA

Closing Remarks

Ashley Hofmann

Market Outreach

PCS


Drinks
Reception
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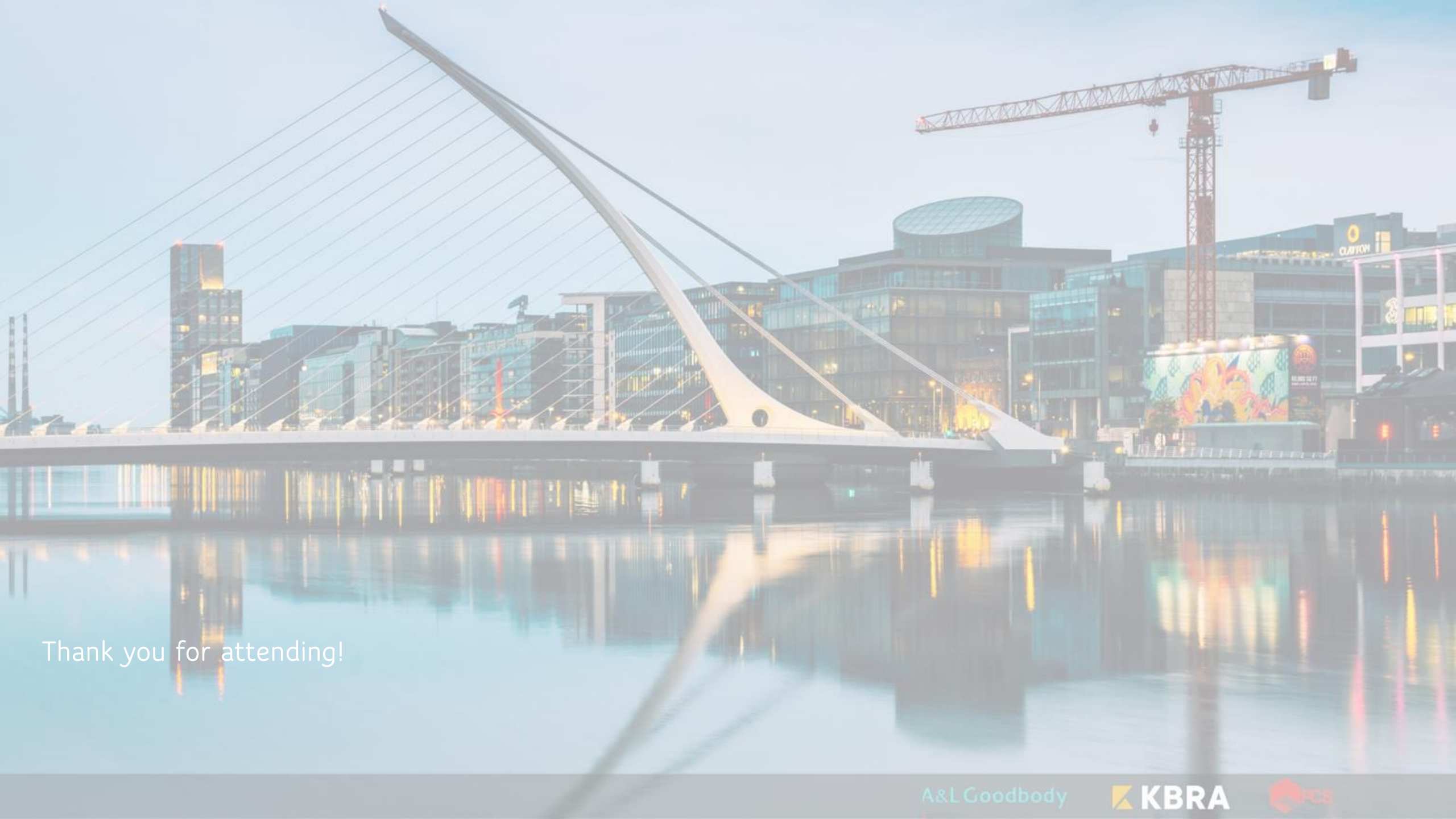

Thank you for attending!