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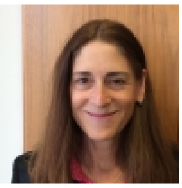
Securitisation: is the EU proposal up to the challenges?

Speakers

Alexander Batchvarov
Bank of America Merrill Lynch Global Research , PhD, CFA, Head of International Structured Finance and Covered Bond Research



Katherine Frey
Moody's Investors Service , Managing Director-Structured Finance

Michel Heijdra
Ministry of Finance, the Netherlands , Regulatory Strategy and Member of the Group Management Committee

Xavier Larnaudie-Eiffel
CNP Assurances , Deputy General Manager

Mario Nava
European Commission , Director for Regulation and Prudential Supervision of Financial Institutions, DG for Financial Stability, Financial Services and Capital Markets Union

Paul Tang
European Parliament , MEP, Committee on Economic and Monetary Affairs

Roman Turok-Heteš
Ministry of Finance, Slovak Republic , Director General, Financial Market Section

Pablo Zalba Bidegain
European Parliament , MEP, Vice-Chair of the Economics and Monetary Affairs Committee

Steve Hottiger
UBS AG , Head Group Governmental Affairs

Objectives of the session

The session tried to clarify the ambitions and the expected contribution of the EU securitisation framework in the EU Capital Market Union context. The session also outlined how to make effective progress toward an efficient and consistent EU securitisation framework. In particular, the session addressed the risk specificities of securitisation techniques as a prerequisite to achieve an accurate calibration of the framework.

Executive Summary

Background to the Securitisation Proposal

The securitisation market was not only about how much was issued, but what was issued, what was placed, how many were buying, how many people traded, and what the secondary volume was. There was no single metric showing a positive development. Volume was in decline: 15 billion had been placed in Q1 2016, with 35 billion of retained issuance. Primary supply continued to be net negative, meaning the market was shrinking. In the last few months, four broker dealers and market makers had been lost, a trend which was continuing. Half of the research houses from five or six years previously were left, reducing market transparency and coverage. A reduction in trading, research, inventory and in-house infrastructure was very difficult to restore. There was also concern about two effects that were very specific to Europe: the sovereign cap and the tranche maturity.

In 2005, market issuance had been around €320 billion of European securitisation. In 2015, levels had been roughly two thirds of those in 2005. For auto ABS, which was the largest chunk of this, issuance was around €7 billion in 2005 and €35 billion in 2015. That segment of the market was functioning fairly normally, where debt was placed with real investors; the CMBS and SME portions of the market, though, remained quite small.

Securitisation ticked many of the boxes of Capital Markets Union. For large banks that had the choice of issuing unsecured debt, tapping into covered bond programmes or using securitisation platforms was just one of many options. However, for small- and medium-sized banks and other small financial institutions, it was a primary source of funding. Securitisation also enabled banks to manage their balance sheets and recycle capital. Getting securitisation regulation right was critical, and time was of the essence. Expertise was leaving the market, and it was important to get this right. Furthermore, at present, many SMEs were too dependent on banking finance. A strong and profitable banking industry was needed in Europe, so this was a key moment to launch the CMU.

The issues that regulatory proposal needed to address

It was important to have true recognition of the risk transfer in securitisation, as securitisations were generally quite an expensive form of funding. In actuality, experience of dealing with regulators suggested that it was very difficult to prove that no remaining risks or rewards stayed with the bank. The Basel capital calculation had been done in a very opaque way. The negative ‘c’ in the ‘p’ factor in the IRB formula was one example. Taking complexity and structural risks into account in terms of capital charges on the whole waterfall, might make sense to a certain extent, but the reduction of those risks via the conditions set by the STS regime should also be taken into account and lead to a relief of this extra capital cost. It was also important that STS securitisations had equivalent treatment to similar instruments. AA treatment, at least, should be achieved from a liquidity perspective, such as covered bonds, in all LCR determinations.

Insurers had more liability than asset managers, and for them this period had been quite difficult. Securitisation would not be bought if it was either more complex or riskier than other classes. The simpler it was, the easier it was to put money into. Compared to covered bonds, securitisation in Europe was not at all competitive. Securitisation was the only class of asset where there was a risk of criminal sanctions; therefore, covered bonds would be the preference. There should be real proportionality in terms of the sanctions to market participants linked to due diligence, whenever they acted in good faith; this should be recognised and credited. Penalties should only be applied in cases of negligence or deliberate misconduct.

The functioning of the secondary market was also important. The Commission should ensure that the market transparency requirement and other rules impacting market-making were fully aligned with the objective of the CMU. Borders should be opened up to make sure that securitisations were open to non-EU investors and originators. Only then would there be stronger capital markets in the future.

Sensitive issues related to securitisation

The proposal was to take the prospectus and securitisation into a dialogue in Parliament soon. There was a constructive attitude in the European Parliament. However, building a political and broad majority in the Parliament would take time, given the level of detail. In addition, the lessons of the past needed to be learnt, not only for explaining it to the public, but to reach a majority in the Parliament.

Securitisation had two functions: to be a stable source of finance, and to be able to transfer risks from banks to other financial institutions. Looking at the past performance of the market, it had been less than stable. It was now approximately one tenth of pre-crisis levels, and it had nearly halved from 2008 to 2009. New issuance had decreased dramatically from pre-crisis levels. The difference between failure rates in the EU and the US was staggering. The same went for the transfer of risk. Securitisations were now seen, but they were largely retained.

The incentives needed to be examined from the investor side, but also from the supply side. However, if capital charges were higher and it was more complex, it was not clear that investors would enter this market.

Securitisation was indeed toxic in most people's minds, but it meant different things in Europe and the US. The default rates of AAA securitisation products in the EU, at the start of the crisis, had been 0.1%, compared to 16% in the US. In addition, after the crisis, European regulators had introduced significant restrictions in underwriting standards. The fact that underwriting standards had been restricted effectively meant that it would be difficult to create a bad product to go into securitisation.

Two things were being conflated within the word 'securitisation'. The results of the securitisation of the US were fundamentally different from those in the EU. One type of securitisation could be separated from the other by the introduction of criteria, some of which were fundamentally different to those in the US, such as the requirement for 'skin in the game', the diversification requirement and the transparency requirement. STS capital requirements in the EU were already more ambitious than at an international level. A convergence with the US was positive, but it needed to be debated. The Commission, having produced these criteria, had enabled the international discussion to evolve.

According to the agreed schedule, they would pass both regulations in the European Parliament in November. They were at a key political moment, and could not afford delays in the dossier. What mattered was that it was being looked at carefully. If the work of the Parliament was such that it increased the appetite for STS, this would be positive. However, it was also not clear that removing the stigma alone was sufficient to make the market stable.

Potential Solutions

There were two levels: the political and the technical. There was no doubt that at the technical level there would be close co-operation and solutions would be found easily. Among the different responses of the industry, there had been quite a few workable proposals as to how to address some of these issues. The point, however, was that the stigma made the political debate very difficult.

Despite talk of toxic securitisations, this was really a portion of the market where the risk had been emanating from the US housing market. In Europe, less than half of 1% of rated securitisations had suffered any principal loss, and that had been during a period of extreme economic stress.

Finally, there was not concern around the direction of travel, but around whether the destination would be reached.

Detailed Summary

Introduction

A crossroads had been reached in the securitisation market. For example, the previous year had been the first in which more covered bonds than securitisations had been issued in the Netherlands. On the one hand, this demonstrated that the covered bond market was starting to work in the Netherlands. However, at the same time it demonstrated that another market, which had used to be the key to financing the real economy, was simply no longer there. What was the situation now, and what should be done about it?

Background to the Securitisation Proposal

The state of the securitisation market

A banker said that the securitisation market was looked at in several different dimensions. It was not only about how much was issued, but what was issued, what was placed, how many were buying, how many people traded, and what the secondary volume was. A single metric for these had not been successfully developed.

Volume, in terms of issuance, was declining. 15 billion had been placed in the first quarter 2016, which was the lowest volume for five or six years – not to mention before the crisis. 35 billion of issuance had been issued not to be placed on the market. This was basically building up ECB repo inventory. Thirdly, the primary supply continued to be net negative. In other words, less was being issued than was amortising, so the market was shrinking, gradually or more rapidly depending on the sector. Inventory by trader was declining. In the last few months, four broker dealers and market makers had been lost. There was a risk of this trend continuing. The transparency of the market was also declining. There were at present roughly half of the research houses that had existed five or six years previously, which was reducing market transparency and coverage.

The big question was whether the point of no return was being reached, and how this could be reversed. When there was a reduction in trading, research, inventory and in-house infrastructure, it was very difficult to restore and recover.

The causes of the problem

Regulation was one of the factors, but there were other market factors driving the change, and there were several issues that needed to be addressed. The markets were continuous and fluid. One market could not be wished to recovery by magic, at the same time as another market was being treated favourably. There should be continuity and balanced treatment of the risks of different products across the spectrum. It could not be argued that securitisation contributed to the originate-to-distribute model and was therefore bad, when at the same time the sale of whole loan portfolios was being forced, which were an originate-to-distribute model in a different guise, and this was being claimed as good. It could not be argued that an originate-to-distribute model was creating more risk, because this was not confirmed by data such as the studies of the Central Bank of Italy or the Atlanta and Boston Feds.

The other aspects of the market were seeing increasing fragmentation. Currently, market fragmentation occurred between the repo-eligible and the LCR-eligible. At present in terms of market development, the non-STS market was working. There was quite a bit of issuance there, and most of the placement was full placement of capital structure from AAA to equity. This was not the case with what would supposedly fit into the STS category. In this respect the STS Commission proposal was intended to promote 'good quality' securitisations and a more risk-sensitive regulatory capital treatment, and therefore promoting cross-border securitisation transaction markets.

Finally, there was a need to look at regulation holistically. Capital was one requirement, but the other requirements mattered on a comparative basis. There were three concerns. The first was that Europe was taking over the Basel regulations. The Basel capital calculation had been done in a very opaque way and, from the perspective of those who worked with those products, it was not clear how many inputs had been derived in the formulae. The negative ‘c’ in the ‘p’ factor in the IRB formula was one example. This negative ‘c’ could reduce capital when a portfolio had a worse credit quality. The question needed to be raised about transparency and the actualisation of the information used in that calculation.

There was concern about double-counting and non-neutrality. The opposition was not to non-neutrality in the securitisation calibration, but it did not make sense to be unconstrained. There was also concern about two effects that were very specific to Europe: one was the sovereign cap, which would affect securitisation particularly for rating-based capital, and the second was the tranche maturity, which had specific legal ramifications for different countries in Europe, based on insolvency regimes and other aspects that were discussed in previous panels.

Before and after the crisis

A market participant representative noted that, in 2005, market issuance had been around €320 billion of European securitisation. Importantly, that debt was all placed with real investors. Half was RMBS, which was mostly in the UK, with the Netherlands as the second most common location. There was a lot of Spanish and Italian issuance. CMBS was a decent-sized market, and in the ABS consumer space there were pools of securitisation full of loans to consumers, whether auto ABS, credit cards or unsecured consumer loans. That was about €20 billion. The SME lending portion of that market was relatively small, at less than €10 billion.

In 2015, levels had been roughly two thirds of those in 2005. Some would argue that this was a reasonable volume for a healthy, sustainable market. The problem was that only a third of this had been placed with real investors, so two thirds of the issuance had been retained or used as repo for central bank funding. Half of the issuance again had been RMBS. Notably, the next largest sector had been the ABS consumer sector. This was one sector that had, in fact, grown over the last decade versus the crisis. For auto ABS, which was the largest part of this, issuance was around €7 billion in 2005 and €35 billion in 2015. That segment of the market was functioning fairly normally, where debt was placed with real investors. CLOs had returned in some strength over the last couple of years, and the issuance was just under €25 billion. CMBS and SME portions of the market, though, remained quite small.

Capital Markets Union

The essence of the CMU was to diversify and increase funding possibilities for companies in the EU and in particular for SMEs, to promote alternative sources of funding and to complement in this respect the banking sector. Securitisation ticked many of these boxes, which was why it was obviously such an important topic. It provided disintermediation and an alternative bank funding source. For large banks that had the choice of issuing unsecured debt, tapping into covered bond programmes or using securitisation platforms was just one of many options.

However, for small- and medium-sized banks and other small financial institutions, it was a primary source of funding. It was a critical source of funding for organisations like auto-captives, some of the new platform lenders and challenger banks. Securitisation also enabled banks to manage their balance sheets and recycle capital, which was very important.

The market at present

One of the most talked about deals in recent months had been a UK RMBS deal priced earlier in April. This had been a securitisation of around £6 billion. It had been around 80,000 individual mortgage loans initially originated by Northern Rock, before the crisis. This portfolio had found its way onto the UK balance sheet during the crisis, and had effectively now moved off balance sheet and been placed predominantly with investors; around 80% were non-European investors who had been looking to diversify their portfolios and yield. This had been a very effective and successful transaction.

The preceding week had seen the launch of the first European marketplace deal, through which the platform funding circle had been looking to obtain financing so that they could continue to lend into the UK SME space. Moreover, given the market storm since the emissions crisis began, Volkswagen had been heavily relying on the securitisation market for funding auto ABS. Since September they had issued around €6 billion debt in Germany, Spain and the UK. They had also issued in Japan, China, Australia and Brazil, via all the other ABS auto markets. Spreads were higher, but investors had been there and the market open.

Securitisation as a tool was a critical part of a well-functioning capital market. Getting the regulation right was critical, and time was of the essence. Expertise was leaving the market, and it was important to get this right.

Views on Securitisation

Credit rating agencies were of the opinion that the devil was in the detail, and none of it could be certified. Auto ABS should, in its simplest form, qualify for STS if there was no RV risk – as should a very basic RMBS structure.

The industry perspective

A banker said, from the perspective of an originator, it was important to have true recognition of the risk transfer in securitisation, with full capital relief obtained. Securitisations were generally quite an expensive form of funding, if a bank had a decent rating, so the risk transfer needed full recognition in terms of its capital treatment, not less than for any other funding instrument including covered bonds. In actuality, experience of dealing with regulators suggested that it was very difficult to prove that no remaining risks or rewards stayed with the bank, and as such to have the full capital relief expected.

In terms of capital and liquidity treatment, it was also important that STS securitisations had equivalent treatment to similar instruments, from a liquidity perspective, such as covered bonds, in all LCR determinations. AA treatment, at least, should be achieved.

It was important that the capital treatment of these securitisations, both absolutely and relatively to alternative instruments, ensured that there was a level playing field for securitisations. The risks that mattered were not the type of structure, which was a key driver for prudential treatment. In terms of the capital charges on the whole waterfall, to a certain extent it might make sense, taking complexity and structural risks into account. On the other hand, the reduction of those risks, via the conditions set by the STS regime, should also be taken into account and lead to a relief of this extra capital cost.

The aspect of due diligence and sanctions was also worth mentioning. The verification requirements placed on the investor side were an operational burden. Combined with the uncertainty around designation and exposure to punitive fines if something went wrong, it did not lead to much appetite on the investor side. There should also be real proportionality in terms of the application of sanctions to market participants who acted in good faith; this should be recognised and credited. Penalties should only be applied in cases of negligence or deliberate misconduct.

Capital Markets Union

Finally, the functioning of the secondary market was also important. Market-making in securitisation bonds should be allowed to function effectively in order to ensure a reasonable level of secondary market liquidity. In this context, the proposed MiFID II non-equities transparency regime could have a detrimental impact on secondary market liquidity for securitisations. The Commission should ensure that the market transparency requirement and other rules impacting market-making were fully aligned with the objective of the CMU in this context.

It was important for CMU to be, to the extent possible, created without borders. One lesson from the crisis was that the tendency to think nationally and regionally first, in an effort to restore financial stability from home and guard against financial instability, had somehow disrupted the flow of global capital. Making Europe even more dependent on deleveraging the domestic banking sector was not at this point helping to revitalise the market. From that perspective, borders should be opened up to make sure that securitisations were open to non-EU investors and originators.

A national public decision maker, in response to why they had a complicated structure for third-country recognition, had said that they had wanted to help the US regulators for once, who had been against the proposal. It was of the utmost importance to have open capital markets. Only then would there be stronger capital markets in the future.

The insurance view

An insurance industry representative noted that insurers had more liability than asset managers, and had to develop skills in asset liability management. For them, as everyone else, this period had been quite difficult. Everyone would be delighted to be able to choose from a variety of asset classes, providing a diversification of portfolios as well as hopes for some returns.

Life was difficult for CFOs, CEOs and those people who signed authorisation to invest in one class or another, as well as for investment specialists. There was no opposition to securitisation; and whenever being active outside the EU a level playing field would be necessary. That being said, life was complicated enough, so they would not buy anything in securitisation if it was either more complex or legally riskier than other classes. Though insurers welcomed the STS motto to achieve simple securitisation, but what did ‘simple' mean? It meant a generally characterised product, whose contents were well understood. The simpler it was, the easier it was to put money into. Too many diverse tranches or different models were undesirable, and it would be useful to have help, perhaps from a third party, to tell everybody whether a product was effectively STS or not.

Insurance companies would be more interested in STS than other products. Safety was paramount when investing; the return was one thing, but it was less important than the safety of investments. It needed to be simple, and competitive against other sources or classes of assets. Technicians were best able to develop this, but it was fair to say that, even if things might have progressed, the calibration of Solvency II regarding securitisation, rather than Basel III still needed to be undergone. Compared to covered bonds, securitisation in Europe was not at all competitive.

Large insurance companies exerted some form of due diligence on each of their investments. However, insurers did not want red tape; they had good processes, and would exert their processes for securitisation as well as for other classes of assets. Securitisation was the only class of asset where there was a risk of criminal sanctions. Of course, it was very remote; it had been vetted by the Commission, the Parliament and the Council, but the risk was still there. There would be no sanction if covered bonds were taken, therefore covered bonds would be the preference. It was a simple as that.

Finally, if the instrument was not able to be brought back to true competitiveness, then there was no use in discussing it.

The Process

The forthcoming Slovak presidency

An official said that, during Slovakia's presidency, the EU Parliament would have to begin to tackle this file. It had already set up a responsible team to deal with securitisation, but they were also considering the revision of the Prospectus Directive, as one of the main pillars of the CMU. The proposal was to start a dialogue in Parliament soon on the prospectus and securitisation.

A politician noted that, at the start of this file, it had been said that the proposal for securitisation was seven weeks. The Council had taken seven weeks, which could be seen as a compliment to the

Dutch presidency. At the same time, it showed that it had been dealt with at the technocratic level. Indeed, securitisation was still a toxic product in the minds of many, and the question was whether it had been detoxified. Had the lessons of the past been learnt? This was crucial, not only for explaining it to the public, but to reach a majority in the Parliament.

Slovakia did not have a securitisation market. The Slovak capital market was very weak, and it was expected that securitisation and the whole package of the CMU would help Slovakia to attract more investors and speed up the process of revitalising capital markets. The intention of the forthcoming Slovak EU Presidency was to start with the CMU package as soon as possible.

Combining a stable source of financing and risk transfer

The question was whether it would contribute to a stable financial system. Securitisation had two functions. It needed to be a stable source of finance, mainly for banks, and it needed to be able to transfer risks, preferably from banks to institutions outside the banking sector.

Looking at the past performance of the market, it had been less than stable. Losses in Europe were much less than in the US. However, the market had nevertheless collapsed. It was now approximately one tenth of pre-crisis levels, and in the collapse it had nearly halved from 2008 to 2009. Hence it had not been a stable source of finance. How, then, did it contribute to the stability of the financial system?

The same went for the transfer of risk. Securitisations could now be seen, but they were retained. The banks made a securitisation, and then brought it to the ECB. Of course this was not the intention of the new legislation and proposal. One reason why the banks brought securitisations to the ECB was that they did not want to lose the risk. There was also a return.

The incentives needed to be examined from the investor side, but also from the supply side. There had not been much of an incentive from banks to transfer risks outside of the system, especially when there were plenty of cheap sources of finance and there was still the possibility of covered bonds. The banks were in trouble; they had a business model that might or might not be viable. Why would they throw away a return, even if it was a risk? If the capital charges were higher and it was more complex, it was not clear that investors would enter this market. It made it difficult to create a liquid market, but from a social point of view there was a desire to contribute to stability.

The view in the European Parliament

There was nonetheless a constructive attitude in the European Parliament. Securitisation was the pooling of risk, which had been a tradition in the financial sector. Risk was pooled to help make markets better by allowing people to better bear risk. On the one hand, there were concerns relating to the stability of the market they were seeking to create, but on the other this constructive approach might contribute to market stability through the transfer of risk. Building a broad political majority in the Parliament would take time, because a bridge needed to be found between the two. However, it could be done. It was also a very complicated issue for ‘simple’ parliamentarians. It was not clear who decided what STS was, and so forth. There were many such details, which was why it took time. Hopefully, the first position would be reached before the summer, with the discussion taken further subsequently.

Another politician said that there was definitely a constructive attitude. However, this was a difficult debate for the European Parliament. It must be understood that the difficulties arose from what had been lived through in the last few years.

There was also a need to understand the political context of the present position. Growth and jobs needed to be pushed. At present, it was not easy for many SMEs, who were too dependent on banking finance, in contrast to the US. This was one of the reasons for the importance of capital market union. In the European situation, with low yields, new capital requirements and new financial regulations in place, problems arose for the banking industry and its profitability. A strong and profitable banking industry was needed in Europe. This was a key moment to launch the CMU, and STS and capital requirements clearly worked in that direction.

Failure rates and recovery of securitisation markets in the EU and US

An official observed that the difference between failure rates in the EU and the US was staggering. The default rates of AAA EU RMBS, at the start of the crisis, had been 0.1%, compared to 16% in the US. With BBB products, the default rate had been 0.2%, compared to 62% in the US. There was a phenomenal difference in the performances of the two markets.

Looking at the recovery of the markets, it could be argued that the trends were similar. It could even be argued that, in the last few years, recovery had been more continuous in the US. However, securitisation was 80% public guaranteed, which had helped the recovery of the market. Growth had also returned more quickly in the US.

Definition of STS

The events in the US (and their damaging effects on global securitisation markets) have altered the perception of investors with regard to all securitisation products, without geographical or asset class distinctions. Therefore, one proposal, building on several work streams at EU and global level, was to try to remove the stigma attached to the word ‘securitisation’. One type of securitisation could be separated from the other by the introduction of a set of criteria, able to reduce the risk attached to certain structural features of the securitisation process with particular regard to 'model' and 'agency risks'. These criteria were meant to enhance simplicity, transparency and standardisation of qualifying securitisations. One of these criteria was to comply with EU risk retention rules.

Attitudes beyond Europe

Non-neutrality of capital requirements was an open issue. It seemed reasonable that the higher complexity of the securitisation process and structure would lead to higher requirements in comparison to those applicable to underlying assets. Capital requirements were still a hot topic, and they would certainly be one of the most relevant issues to be debated at the European Parliament. EU was leading the global debate and trying to push other jurisdictions to be as ambitious as possible with regard to the calibration for STS securitisations. Despite the initial scepticism showed by the BCBS Committee in making progress on the issue, important progresses were registered both on the front of the definition of the STS (STC in BCBS/IOSCO language) criteria and on the prudential treatment of (term) STC securitisations. A final decision by the BCBS committee was expected by the summer. The circumstance that certain jurisdictions could finally opt out and not implement the STS framework raised the issue of the treatment of STS securitisations issued in those jurisdictions via mutual recognition/equivalence mechanisms.

The schedule

A politician observed that there was some concern around timing. According to the agreed schedule, they would pass both regulations in the European Parliament in November, and this was expected to be complied with. There was someone to link STS and CRR to EDIS, and someone else to link EDIS to treatment of sovereign debt. However, to link everything was dangerous; the scope of CMU was different to the scope of EDIS: the former was the whole of the EU, the latter the eurozone. If the links delayed the process, there would be trouble; they were at a key political moment, and could not afford many delays in the dossier.

An insurer reported that, from an insurance point of view, there was interest in good securitisation products, provided they were simple and competitive enough compared to others. The negative ‘c’ was less important than the final result. What was the collective capacity to reach that end quickly?

An official underlined the priority that the Council gave to the proposal, being able to agree on a general approach in two months and two days. He also expressed the hope that the EP might be as efficient as the Council in dealing with the proposal. The Parliament was taking a little more than two months and two days. Among MEPs, there was more interest in non-STS than in STS; if the work of the Parliament increased the appetite for it, this would be positive.

A politician reflected that the product was toxic in the minds of people. This stigma had to be removed. It may have been toxic in investors’ minds, but many were now saying that, whether it was simple and transparent or not, they understood what they were buying and had learnt that lesson. It less not clear, though, whether there were alternatives available that they preferred; therefore, it was not guaranteed that removing the stigma alone was sufficient to make the market stable, which was essential.

Potential Solutions

Political responses

A politician stated that negative ‘c’ was very difficult issue for parliamentarians. How to produce a good calibration to make securitisation a viable and stable asset class was a question that needed to be discussed.

Another politician noted that there were two levels: the political and the technical. There was no doubt that at the technical level there would be close co-operation and solutions would be found easily. The point, however, was that the stigma made the political debate very difficult. There needed to be awareness of this, and the European Parliament would listen to many debates, going back to casino capitalism. They were confronted with the precise issues that had created the crisis, and needed to be ready for that: there would be a political influence on the technical work and debate.

Industry responses

A banker reported that, among the different responses of the industry, there had been quite a few workable proposals for how to address some of these issues, including a detailed letter written and prepared by multiple organisations. There was concern not around the direction of travel, but around whether the destination would be reached.

In the detailed letters received, from AFME and other participants, many points had been made, including that SA and ERBA needed to be addressed in the hierarchy of approaches. It needed to be kept in mind that ERBA, even with the proposed reduction, actually increased the capital relative to the present day. More progress was needed on the issue of maturity, and it was strongly believed that the related adjustment did not make sense on a tranche level: an asset created significant differences in the capital treatment between instruments that did and that did not have a maturity adjustment, and it was unclear why.

Capital was only one aspect. It was difficult to invest, given the need to demonstrate due diligence and the possibility of being subject to penalties if something went wrong. A guess had to be made about what was compliant and what was not. These issues needed to be addressed, and the playing field levelled with different instruments. Some of the risks had already been addressed. After the crisis, European regulators had introduced significant restrictions in underwriting standards; the fact that underwriting standards had been restricted effectively meant that it would be difficult to create a bad product to go into securitisation. Securitisation ultimately repackaged loans. All of these different aspects needed to be taken into account, as well as their being laid on top of each other.

Conclusion

Credit rating agencies reflected that, despite talk of toxic securitisations, this was really a portion of the market where the risk had been emanating from the US housing market. There had been very significant and severe problems there. In Europe, less than half of 1% of rated securitisations had suffered any principal loss, and that had been during a period of extreme economic stress across the markets, so the product had worked and worked very well in Europe.

A banker added that, given that the founding component of securitisation was difficult, especially in the current circumstances, it might be worth considering the kinds of tools that allowed the transfer of risks to other counterparties in the investment space and ensured that the framework for different regimes – especially NSFR and the liquidity coverage ratio – did not disallow types of total risk transfers to other counterparties. They would still be punished by having the asset on the balance sheet, and would have to term-fund the whole asset. This took away the economics achieved by transferring the risk to counterparties.