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Securitisation and STS: contribution to financial markets stability in the EU

In order to asses this question, the review of the last financial crisis provides two important insights: First, default rates of European securitisations were consistently low and did not cause losses and bank bailouts. Rather, securitisation as a highly collateralised financing tool has contributed to financing the real economy in times of crisis. Secondly, the European legislator and the ECB have rightly adopted a number of important regulations in the period 2009 to 2011 that will prevent securitisation types that were responsible for the financial crisis 2008, especially: 5% risk retention, loan-level data, no originate-to-distribute models and ban on re-securitisation.

Now how is securitisation used in practice and what impact does the new EU Securitisation Regulation (applicable since 2019) make? Firstly, banks can provide its customers with solutions for funding and capital relief, products employed are public term ABS with placement to investors, and private securitisation financed via bank balance sheets and including ABCP programs (Asset Backed Commercial Papers). Secondly, banks securitize own assets from their ordinary course of business to achieve funding and capital relief. This again involves term ABS as well as private, bilateral securitizations for risk transfer. This differentiation is necessary in order to understand what contribution the EU Securitisation Regulation has made and what problems still need to be solved.

The EU Securitisation Regulation overall and also the STS criteria for simple, transparent and standardised securitisations as a quality segment distinguish between ABCP and non-ABCP (i.e. term ABS). Term ABS issuance of €220bn in 2019 has declined by ca. 15% compared to 2018, and no new issuers or investors could be attracted. On a positive note, STS has gained broad acceptance as new market standard in the asset classes residential mortgages (RMBS), auto, consumer and equipment leasing ABS. This has been supported by the independent third-party verifications of the STS criteria. The strong regulation, acceptance of STS and increased transparency have strengthened confidence of politicians, central banks and supervisory authorities. However, this positive aspect only applies to the Term ABS market.

The picture is different for private securitisations and ABCP, as well as the market for capital relief trades, together making up a volume of ca. €200-250bn p.a. in Europe. The new Securitisation Regulation does not reflect the particularities of these market segments, with sometimes inconsistent, inappropriate and prohibitive rules and reporting obligations. ABCP securitisations should be treated as what they are: Highly secured funding instruments, allowing banks to finance the real economy and receive secured refinancing with short maturities, similar to covered bonds at the longer end of the maturity spectrum. Still a series of changes and improvements need to be made to the level 1 regulation and certain level 2 RTS issued by the respective ESAs. The level playing field of securitisation with other products like covered bonds as part of the Capital Markets Union still needs to be achieved. A clear and consistent ruleset for banks applying significant risk transfer (SRT) for capital relief needs to be established by the legislator and applied uniformly from supervisors across Europe.

Especially in the context of the current situation with severe consequences due to Covid-19 for the real economy and the stability of the financial system, this once again shows the necessity for clear and consistent rules, limited complexity and no procyclical consequences. Under these premises and based on trust, securitisation will contribute to stability and be part of the solution this time.