

## **VDA position on "Defining Liquid Assets in the LCR under the Draft CRR" (EBA discussion paper of 21-02-13)**

### **– Extremely High Liquidity and Credit Quality of Automotive Asset-Backed Securities**

*Automobile banks are an indispensable partner for the motor vehicle manufacturers in the marketing of passenger cars and commercial vehicles. Auto ABS must be classified as extremely highly liquid with high credit quality. Within the framework of the current discussion about new equity requirements for banks, it is therefore absolutely necessary that Auto ABS be able to be included in future in the calculation of the minimum liquidity ratio. Otherwise there is a danger of a severe deficit in the refinancing activities of the automobile banks and therefore an adverse effect on the sales of the German automobile industry.*

On 21st February 2013 the European Banking Authority (EBA) published a discussion paper on "Defining liquid assets in the LCR under the draft CRR". The EBA refers in the paper to Article 481(2) of the draft of the Capital Requirements Regulation (CRR) and adopts a broad interpretation of the assessment mandate derived from it to examine liquid assets: for example, the EBA is also required to analyse other categories of assets that go beyond the criteria specified in Article 404 of the draft CRR.

Against this background, we would like to point out in the following text the importance of so-called Auto ABS for promoting the new vehicle sales of the automobile manufacturers and strongly urge that this form of refinancing be included in the calculation of the LCR.

#### **High quality of the Auto ABS**

Securitisations of automobile loans by captive automobile banks (automotive asset-backed securities = Auto ABS) are characterised by an excellent credit rating and an above-average demand on the capital market. With a figure of around 24.7 billion euros, they contributed 11% to the overall issue volume on the European securitisation market in 2012, making Auto ABS the most marketed asset class. The major portion of the European Auto ABS volume comes from Germany with 57%.

During the finance crisis, the default rate of Auto ABS transactions amounted to almost 0.0%. Auto ABS from the Premium issuers enjoy a very high reputation among investors and are assessed as extremely low-risk investments. A major reason for this, in particular, is that the value development of used vehicles and the default rates of automobile financing have largely remained constant over many years as well as throughout the finance crisis. Auto ABS have therefore proved to be crisis-resistant in

the past and, thanks to their high granularity, they have not caused investors to suffer any losses.

## **Significance of the Auto ABS as a refinancing instrument**

### *Share in refinancing at the automobile banks*

Securitisations of Auto ABS are among the most important refinancing instruments in the groups of companies operating within the automobile industry. Among the German automobile banks, Auto ABS contributed to their refinancing on a scale of between 15% and 50%. It must also be considered that Auto ABS are gaining strength on the European securitisation market contrary to current trends and are also able to record a corresponding development in value. These figures demonstrate the major economic significance of Auto ABS and show that they should not be dispensed with as instruments of refinancing.

In the case of some individual automobile banks, several billions of euros are financed through Auto ABS. If Auto ABS are excluded in the future under the CRR from being taken into account to meet the LCR, it can be assumed that around 30% of the investors on the ABS market will disappear. This would mean that the respective automobile bank would lose several billions of euros of its refinancing funds.

### *Repercussions for the refinancing structure and lending*

Apart from the new liquidity ratios, the new requirements according to Basel III also involve increased equity requirements. Moreover, against this background, it will become more and more difficult for banks to generate regulatory capital, with the result that it will ultimately become more difficult for banks to refinance one another. The refinancing situation of the banks is then additionally worsened if individual means of refinancing are weakened due to a lack of acceptance by the regulatory authorities.

Where individual means of refinancing disappear for the banks, the pressure on the remaining methods of funding available – in particular the deposit business – will increase. The growing competition for deposits then breeds higher refinancing costs again for the banks. The deterioration in the refinancing situation will have a negative impact on the lending capacity and lending policy. As a consequence, the entire automobile industry will be threatened by a weakening of its sales and marketing position. There may also be repercussions for the economy as a whole as a result, by which the small and medium-sized business sector would be among the most affected in its capacity as a supplier to the automobile industry and as bank customer.

### *Liquidity of alternative means of refinancing*

Residential mortgage-backed securities (RMBS) as well as government securities and corporate bonds are to be eligible for inclusion as highly liquid assets. In the present economic climate, however, these financial assets are subject to much higher fluctuations in value than Auto ABS are. The latter are still based on the motor vehicle itself, whereby used vehicle prices have proved to be extremely stable over recent years.

The supposed complexity of ABS transactions in relation to corporate or government bonds is being counteracted by European banks, in particular, through experience gained during the finance market crisis in that simpler structures are being created and uniform standards are being placed on the market governing platforms and the securitisation programmes deployed. These developments are currently still providing for better transparency and greater acceptance, also among investors. So, if RMBS, government securities, and corporate bonds are classified as highly liquid assets, this should certainly be the case for Auto ABS.

*Real economy*

Corresponding effects can also be expected for other branches of the real economy in addition to the automobile industry that finance themselves through ABS (e.g. trade receivables financing). If this refinancing instrument were to be restricted as planned, this would in our view entail a significant weakening of the business effectiveness of companies since ABS cannot be easily replaced by other sources of refinancing.

**Conclusion**

To ensure a solid marketing of motor vehicles, we consider it absolutely necessary that Auto ABS be included as highly liquid assets in the calculation of the LCR. An exclusion of Auto ABS would have a serious negative impact on refinancing and therefore on the sales of the German automobile industry. Consequently, Auto ABS should be assessed in the categorisation into asset classes as assets of extremely high liquidity and of very high credit quality.

Berlin, dated 21.03.2013

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