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The Voice of Leasing and Automotive Rental in Europe

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SPECIALISED CONSUMER CREDIT PROVIDERS IN EUROPE

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Leaseurope & Eurofinas comments on the EBA discussion paper on a STS framework for synthetic securitisations

Eurofinas and Leaseurope, the voices of consumer credit and leasing providers at European level, welcome the opportunity to comment on the European Banking Authority (EBA) discussion paper on a STS framework for synthetic securitisations.

General Comments:

Leaseurope and Eurofinas support the introduction of a new European label for high quality synthetic securitisations in Europe, the so-called Simple, Transparent and Standardised (STS) synthetic securitisations. We believe that the long-term impact of such regime could be positive. We very much welcome the EBA's efforts to produce a discussion paper analysing the rationale of STS synthetic securitisations as well as setting out a list of STS criteria for synthetic securitisations.

Synthetic securitisation is an essential tool for many credit institutions in their credit risk and capital management, so as to facilitate continued lending to households as well as leasing to businesses. It also provides an important asset class for investors seeking to gain exposure to high quality performing bank assets without having to build an origination or servicing platform. The experience to date is that synthetic securitisations continue to be a cost-effective source of capital when compared to other financing instruments.

The development of a sound, stable and wide market for synthetic securitisations in Europe will become even more relevant in the near future as we expect a significant increase in capital requirements for European credit institutions due to the implementation of the finalisation of Basel III. In particular, the new rules are expected to have a considerably negative impact on European leasing companies as the low risk profile of leasing is currently not recognised in the CRR and the new output floor will significantly increase the regulatory capital required to lessors. Consumer credit providers applying internal models for the calculation of regulatory risk will be also impacted due to the introduction of input floors. For these reasons, the availability of synthetic securitisations as an instrument for regulatory capital relief and risk management is key for EU credit institutions going forward.

Finally, we would like to support and endorse the comments provided by AFME as well as the joint comments provided by TSI and the German banking industry, with special focus on their technical comments on the STS criteria.

<u>Responses to the EBA Questions:</u>

Question 1: Do you have any comments on this introductory section of the Discussion paper?

We agree with the observations made in the introductory section of the Discussion Paper. In particular, we agree that it is appropriate to differentiate between "arbitrage" synthetic securitisations and "balance-sheet" synthetic securitisations, and that any proposed STS framework for synthetic securitisations should be limited to balance-sheet transactions.

European business and households should benefit from all options of securitisation markets refinanced credit programs. Synthetic securitisations are an important part of the European securitisation markets and instruments of credit risk transfer and therefore we think they should be included in framework for simple, transparent and standardised securitisations.

We recommend applying the existing STS framework to synthetic securitisations as much as possible, but we understand that in order to reflect the particularities of synthetic transactions, certain adjustments in the STS criteria for synthetic securitisations are required. We think that the same portfolio of receivables should be treated similarly for traditional securitisation (done for funding purposes only, or for both funding and capital benefits in case of a full stack transaction or SRT) and synthetic securitisation ('only' seeking capital and risk transfer).

We would also like to point out that the 2% cap on aggregate exposures to a single obligor in Article 243(2)(a) of the CRR would be unworkable for some of the main types of exposures which are regularly securitised using balance-sheet synthetic securitisation and therefore we think that a concentration limit of 3-4% is more workable.

Question 2: Do you agree with the analysis on the market developments? Please provide any additional relevant information to complement the analysis.

In general, we agree with the observations made in Section 5.2.1 of the Discussion Paper.

Question 3: Do you agree with the analysis of the historical performance? Please provide any additional relevant information to complement the analysis.

In general, we agree with the analysis of the historical performance of synthetic securitisations set out in Section 5.2.3 of the Discussion Paper.

Question 4: Do you agree with the analysis of the rationale for the creation of the STS synthetic instrument? How useful and necessary is synthetic securitisation for the originator and the investor? What are the possible hurdles for further development of the market?

We support the view expressed in paragraph 68 of the Discussion Paper that the changes in securitisation markets in recent years mean that it is now the time to extend the STS framework to include synthetic securitisations. We would like to reiterate the observation at the end of paragraph 66 of the Discussion Paper, that it is important to ensure that any criteria specified for synthetic securitisations are workable and effective, for both originators and investors across the market.

We agree with the "pros" set out it paragraphs 80 to 85 of the Discussion Paper. The main benefit of synthetic securitisations for credit institutions is the transfer of credit risk to third parties when (i) true sale transactions cannot be used due to clients not allowing the credit institution to sell their loans (transfer clause limitations) or when (ii) the analysis of further parameters such as the achievable level of risk transfer, liquidity requirements, transaction costs and timing make a synthetic securitisation more efficient than a traditional securitisation. In addition, synthetic securitisation is a very effective tool for transferring the risk associated with a portfolio of exposures without grossing up the originator's balance sheet at the solo level by needing to issue and retain the senior, low-risk tranches. We believe that there is a need in Europe to use balance sheet synthetic securitisations for risk management and for risk transfer outside of the banking sector.

Regarding the need of synthetic securitisations for investors, it is our opinion that risk transfer products are suited for experienced investors that are required to have the knowledge and careful due diligence. Skilled investors already invest without a STS label therefore it is important to align STS synthetic securitisations with the regulatory treatment of true sale STS securitisations, otherwise we have doubts with the success of this project.

For credit institutions synthetic securitisation is a useful instrument to manage risk in their balance sheet. Regulatory uncertainty, uneven treatment and detailed reporting requirements in a bilateral market are possible hurdles.

Question 5: Do you agree with the assessment of the reasons that could eventually support a preferential capital treatment?

We agree with the "pros" set out in paragraphs 88 to 92 of the Discussion Paper. In particular, just as is the case for traditional STS securitisation, given that the criteria for synthetic STS securitisation will result in a simpler, more standardised and more transparent product, the preferential capital treatment is justified. This is particularly the case in light of the analysis of the historical performance of existing synthetic securitisations, even without the additional protections that would be offered by the STS framework.

It is also worth noting that lower risk weights for banks and insurers acting as investors as well as the preferential liquidity treatment provided under the LCR regulation have been the main drivers for the acceptance and implementation of the STS label in “traditional” securitisations.

Question 6: Please provide any additional relevant information on potential impact of the creation of the STS synthetic securitisation on (STS) traditional securitisation, and any other information to complement the analysis.

In our view, the creation of a STS framework for synthetic securitisations will make securitisations markets overall stronger. Having a STS label for synthetic (risk transfer) and “traditional” (funding and potentially risk transfer) securitisations will ensure that the choice between them will be part of banks’ capital management strategy. We do not expect that the creation of a STS label for synthetic securitisations will have any negative impact on true sale STS securitisations.

Question 13: Do you see a justification for possible introduction of a differentiated regulatory treatment of STS synthetic securitisation? If yes, what should be the scope of such treatment and how should it be structured – for example only for senior tranche retained by the originator bank, or more limited/wider?

Question 14: What would be the impact if no differentiated regulatory treatment is introduced? In that case, is the introduction of the STS product without differentiated regulatory treatment relevant for the market?

We strongly believe that introducing a differentiated regulatory consideration for synthetic STS securitisation is appropriate and will contribute to the continued development of this important segment of EU financial markets. We think that introducing a STS framework for synthetic securitisation without a differentiated regulatory treatment will have a limited positive impact. The framework will be far more successful in rapidly achieving its goals of ensuring greater simplicity, standardisation and transparency across synthetic securitisation transactions if the additional operational and economic burdens associated with compliance with the STS requirements can be mitigated by the preferential risk weights that apply to traditional STS securitisations.

Question 15: What would be the impact of potential differentiated regulatory treatment from level playing perspective with regard to third countries where STS framework has not been introduced?

Balance sheet synthetic securitisation is a tool which has been used by EU banks far more extensively than banks in other jurisdictions. As such, we consider that any adverse impact on the "level playing field" resulting from providing for a preferential regulatory treatment for synthetic STS securitisations for EU credit institutions would be relatively limited.

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About us

The membership of our two Federations covers institutions specialised in one or more of the following activities:

Lending to consumers, for instance via personal loans, credit cards or lease/hire purchase agreements; leasing to businesses of all asset types, including machinery and industrial equipment, ICT and others assets; motor finance, granted to individuals or businesses, either in the form of loans or leases.

The consumer credit, asset finance and leasing markets have developed to respond to business investment and consumption needs as well as to accompany the development of local industrial production and distribution. The types of institutions represented by the Federations include specialised banks, bank-owned subsidiaries, the financing arms of manufacturers as well as other, independently-owned institutions.

Specialised financial services providers across the European Union (EU)/European Economic Area (EEA) encompass a diversity of organisations of different legal nature (i.e. credit institutions, financial institutions) and with various operational characteristics (independent companies, subsidiaries of banks, captive finance companies of manufacturers). All share a very high degree of specialisation and have a very limited mix of business activities compared to traditional mainstream banking organisations.

In 2018, the leasing firms represented through **Leaseurope's membership helped European businesses invest in assets worth more than 386 billion EUR**, reaching 833 billion EUR of outstandings at the end of the year[1]. Leasing is used by more European SMEs than any individual category of traditional bank lending taken altogether (around 46% of all European SMEs make us of leasing which is more than any other individual form of lending)[2] and is also popular amongst larger corporates[3]. It is also useful to support the public sector (e.g. leasing to schools, hospitals, etc.).

In 2018, consumer credit providers that are members of **Eurofinas helped support European consumption by making more than 466 billion EUR goods, services, home improvements and private vehicles available to individuals**, reaching 1.1 trillion EUR of outstandings at the end of the year[4]. Consumer lending is procyclical and is highly positively correlated with households' disposable income[5]. By providing access to finance to individuals and households, consumer credit supports the social and economic well-being of millions of consumers across Europe.

Eurofinas and Leaseurope are entered into the European Transparency Register of Interest Representatives with ID n° 83211441580-56 and 430010622057-05

[1] Leaseurope 2018 Annual Statistical Enquiry
[2] Oxford Economics, *The Use of Leasing Amongst European SMEs,* 2015;
European Investment Fund, The importance of leasing for SME finance, 2012;
European Central Bank, Survey on the Access to Finance of Enterprises in the euro area, June 2018
[3] European Central Bank, Survey on the Access to Finance of Enterprises in the euro area, June 2018
[4] Eurofinas 2018 Annual Statistical Enquiry
[5] Eurofinas, *Consumer Credit, Helping European Households Finance their Tomorrow,* 2015