European securitisation: could the market rebound despite COVID-19?

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Global financial markets have undergone a seismic correction over the last few months in the midst of the Covid-19 pandemic. The securitisation industry is not an exception to this as market participants attempt to navigate as best they can the volatility and unpredictability of the situation. **Karen Lomax** and **Jason Bond** from HSBC Issuer Services **and Nigel Batley** from HSBC Structured Finance share their insights into some of the major trends and dynamics currently impacting the securitisation ecosystem.

A market on ice

Even before the acute seriousness of Covid-19 became a reality, issuances of European primary market securitisations had suffered a marked contraction. According to the Association for Financial Markets in Europe (AFME), there were €28.9 billion of primary market securitisation issues in Europe between January and March 2020, corresponding to a 6% year-on-year decline in issuance volumes when benchmarked against the same period in 2019.[1] Moreover, Q1 issuances levels were 42% lower than what they were in 2018.[2]

The pandemic's impact and the rapidly worsening economic growth projections have resulted in a further drying up of issuances in primary market securitisations, a point made by **Nigel Batley, Global Head of Structured Finance at HSBC**. "Excluding a small handful of organisations who have issued paper to themselves only to repo it out, public issuance volumes have been exceptionally low since March 2020. That said, we are seeing some renewed appetite from asset managers such as hedge funds in the secondary market, "says Batley.

Notes:
1. AFME (April 2020) Initial Impact of Covid-19 on European capital markets
2. AFME (April 2020) Initial Impact of Covid-19 on European capital markets

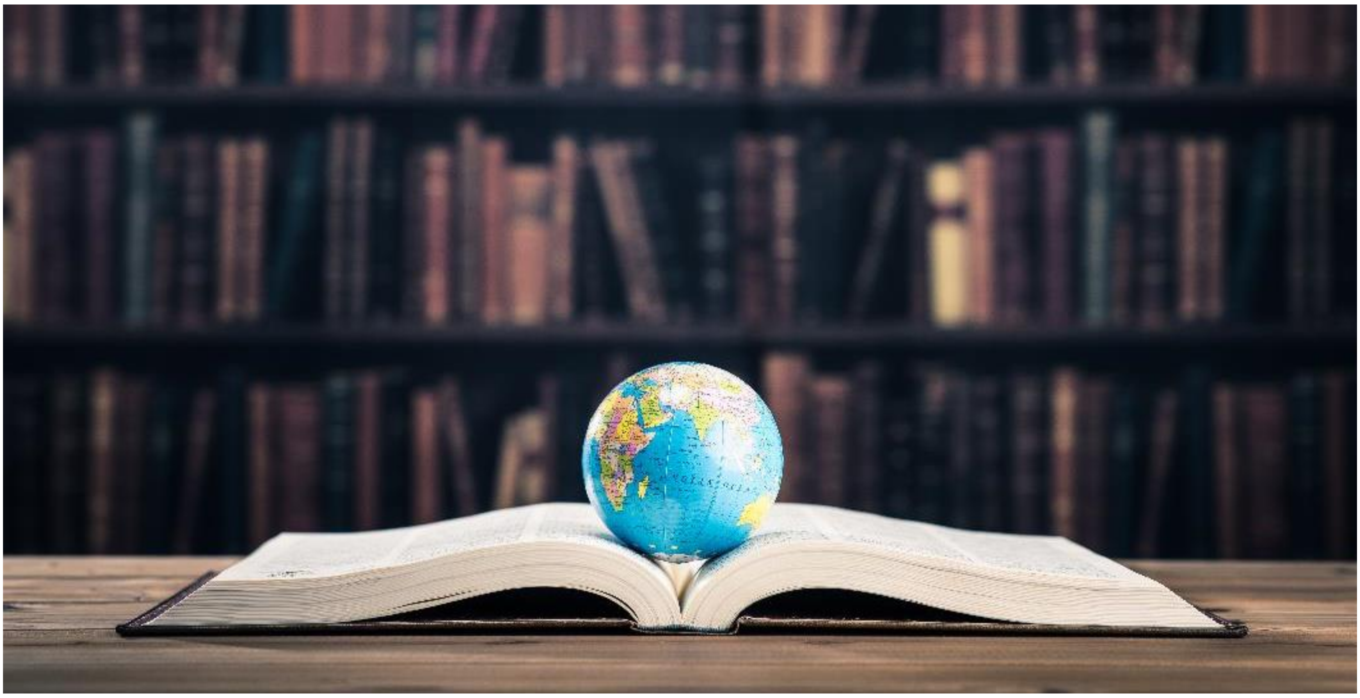
Karen Lomax, Head of Issuer Services, Europe at HSBC, concurs that securitisation activity has dissipated in recent months. "Over the last year, we saw a lot more interest in commercial mortgage backed securities (CMBS). However, real estate is particularly exposed to Covid-19 disruption, so the CMBS market is likely to be substantially impacted," she says. Similarly, Lomax concedes that sales and purchases of non-performing loans (NPLs) - which hitherto had enjoyed buoyant investor interest - were now on pause owing to Covid-19.

Other types of asset backed securities (ABS) products are directly exposed to the consequences too. As companies face sharp revenue compression and even existential crises, the market for collateralised loan obligations (CLOs) has declined significantly, says Lomax. In the US, CLO issuance volumes fell by 48% during Q1 2020 to $15.2 billion, versus $29.3 billion in Q1 2019.[3] Conscious of the rising credit risk at a number of corporates, future CLO issuances are likely to adopt tighter covenant structures to accommodate for any potential deteriorations in credit quality.[4]

A market reshaped by regulations

The securitisation market in the EU is facing a significant shake-up as a result of the STS (Simple, Transparent, Standardised) Securitisation rules, a piece of regulation designed to stimulate issuance activity by providing generous capital treatment to securitisations that meet the basic STS criteria. Even prior to the Covid-19 outbreak, STS securitisation issues in the EU had not met expectations, with STS transactions accounting for just 22% of all public deals in Q1 of 2020, a substantial decline from Q4 of 2019, when that figure stood at 68%.[5]

Notes:
3. Reuters (April 17, 2020) CLO issuance falls 48% as rush of loan downgrades threatens investor distributions
4. S&P (April 2020) CLO spotlight: Redesigning the CLO blueprint after COVID-19
5. AFME (April 2020) Initial Impact of Covid-19 on European capital markets



This inactivity has been exacerbated by the uncertainty which has plagued the STS regulation, most notably around the disclosure and data requirements contained in its reporting template. "One of the biggest impediments facing the STS regulation is its reporting template, an aspect which requires further clarification," says Batley. Lawyers concur users could be deterred from issuing STS securitisations because of the sheer volume of data that needs to be submitted, in addition to the operational complexities of reporting details of cross-border transactions to multiple EU regulators.[6]

"When the STS first came out, it excluded certain asset classes such as synthetics. New STS provisions have since been proposed by the European Banking Authority (EBA), and these are applicable to synthetic securitisations," comments Lomax. In a statement issued in May 2020, the EBA said it would look to apply the principles of "simplicity, transparency and standardisation" to synthetic products just as it had done with traditional securitisations.[7]

This could enable certain synthetic products to benefit from better capital treatment and even allow them to use some excess credit spread for credit enhancement.[8] However, the EBA confirmed that its proposals would be strictly limited to balance sheet securitisations.[9]

Notes:
6. Reed Smith (February 11, 2020) The EU Securitisation Regulation – one year on
7. EBA (May 6, 2020) EBA proposes framework for STS synthetic securitisation
8. Global Capital (May 7, 2020) EBA proposes framework for synthetic securitisation
9. EBA (May 6, 2020) EBA proposes framework for STS synthetic securitisation

Supporting clients through Covid-19

Despite the unprecedented disruption generated by Covid-19, the securitisation market is in an irrevocably stronger position than it was in 2008, something which Lomax says has been facilitated through enhanced transparency and stringent risk retention requirements. Similarly, advancements in technology have also made it much easier for service providers to communicate virtually with their clients. "Technology has helped us support our clients through this tumultuous period. In terms of managing transactions, we now use Zoom which enables us to participate in interactive client meetings. I imagine remote working set-ups are likely to persist for quite some time yet," says Batley.

However, long before the pandemic, HSBC Issuer Services had already adapted its business model to cater to its clients' evolving demands, adds Batley. "Issuer Services are a pivotal participant in the securitisation market. In securitisation transactions where a special purpose vehicle (SPV) is required, our colleagues from Issuer Services provide services which help the client focus on more strategic aspects of the transaction, such as a cash manager, calculation agent or trustee. Not only does this reduce the risk of errors, but it ensures cost synergies are realised during transactions," states Batley.

Making reporting seamless

HSBC Investor Reporting portal

In June 2020, HSBC Issuer Services launched its new Investor Reporting platform, which is designed to provide clients with seamless information sharing and reporting functionalities. The mobile-friendly platform will provide clients with a personalised dashboard module, giving them easy access to new reports and transaction information. "The HSBC Investor Reporting Portal is compatible with smartphone technology, so information can be easily obtained on the move. In addition, smart alerts will keep our clients up to date with any changes in their portfolios," says **Jason Bond, Head of Issuer Services Analytics, at HSBC Issuer Services**.

The portal will also enable clients to manage their transactions more effectively through a dedicated portfolio module. The inclusion of API architecture means clients can extract data in a way that is most compatible with their own infrastructure. The new portal complements the services the offered by the Issuer Services Analytics team. "We have hired specialists from across the market to build an Issuer Services analytical centre of excellence, providing clients a comprehensive service to meet their various data needs," says Jason Bond, Head of Issuer Services Analytics, at HSBC Issuer Services.

To find out more about HSBC Investor Reporting portal, please download the brochure or read the press release.

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