"Restarting the SME credit market in Europe: what role for securitisation and the capital markets?"

9 April 2013
Welcome Speech

Othmar Karas, MEP
Roundtable
Moderated by Othmar Karas and Corien Wortmann-Kool, MEPs

- Alessandro Tappi, Head of Guarantees, Securitisation & Microfinance, European Investment Fund
- Richard Hopkin, Managing Director in the Securitisation Division, AFME
- Vilmos Budavari, Unit SME access to finance, DG Enterprise and Industry, EU Commission
- Emmanouil Schizas, Senior Economic Analyst, ACCA
- Gerhard Huemer, Director Economy Policy, UEAPME
Alessandro Tappi
Head of Guarantees, Securitisation & Microfinance, European Investment Fund
The European Investment Fund

Restarting the SME Credit Market in Europe
Brussels, 09 April 2013
A few key facts about us...

We’ve supported over 1 Million SMEs over 15 years

<table>
<thead>
<tr>
<th>1994</th>
<th>2000</th>
<th>Shareholders</th>
<th>AAA-rated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Founded and started providing <strong>venture capital</strong> to European businesses in 1997</td>
<td>Majority owned by the European Investment Bank (EIB)</td>
<td>62% EIB, 30% EC, 24 public and private <strong>financial institutions</strong> holding the remaining 8%</td>
<td>We’re AAA-rated by all major rating agencies, with a <strong>strong</strong> capital base</td>
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</table>
Helping Financial Institutions to lend more…

“..by using our own capital to credit enhance tranches of SME loans or lease securitisation transactions placed on the capital markets”

<table>
<thead>
<tr>
<th>Guaranteeing</th>
<th>Stimulating</th>
<th>Focusing</th>
<th>Committed</th>
</tr>
</thead>
<tbody>
<tr>
<td>senior and/or mezzanine risk tranches</td>
<td>lending by letting Financial Institutions benefit from our credit quality and capital treatment</td>
<td>on deals with SME portfolio exposures</td>
<td>EUR 2bn of credit enhancement transactions since the financial crisis in 2008</td>
</tr>
</tbody>
</table>
We manage programmes for the EC to deploy SME funding to **promote entrepreneurship and innovation** across Europe.

<table>
<thead>
<tr>
<th>The Competitiveness &amp; Innovation Programme (CIP SMEG)</th>
<th>The Risk-Sharing Instrument (RSI)</th>
<th>Progress Microfinance</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Available budget of over EUR 600m</td>
<td>▪ Pilot project launched in Dec-2011</td>
<td>▪ EUR 200m provided by the EC and the EIB</td>
</tr>
<tr>
<td>▪ Committed budget of EUR 420m expected to mobilise EUR 7bn</td>
<td>▪ Targeting innovative and research-oriented SMEs and small mid-caps</td>
<td>▪ Supporting micro-enterprises and the social economy</td>
</tr>
<tr>
<td>▪ 53 transactions signed in 20 European countries</td>
<td>▪ Total loan volume expected to be generated: EUR 2.5 bn</td>
<td>▪ More than 50% committed at June 2012</td>
</tr>
</tbody>
</table>
EIB Group’s support to SME Debt Finance

Challenges for Banks
- Funding
- Capital

Challenges for SMEs
- Credit risk
- Cost of financing

New lending

Banks

Capital Relief
Term Funding

SME Securitisation

Senior
Mezzanine
Junior

ABS investments

SMEs

Loans for SMEs

EIB instruments
- Loans for SMEs
- ABS investments

EIF instruments
- Credit enhancement
- Portfolio guarantees
- Funded risk sharing
EIF as “deal facilitator” for SME-backed transactions
- Credit enhancer of mezzanine and senior tranches, either with embedded or bilateral guarantee
- Unconditional, irrevocable guarantee of timely payment of interest and ultimate repayment of principal
- Involvement at an early stage of the transaction, always with an independent due diligence role

Own Funds Portfolio (as of 31/12/2012)
- Outstanding commitment: EUR 2.6 bn
- Number of outstanding transactions: 56 deals

Transactions executed in 18 countries, including multi-country/multi-originator transactions
EIF provides an unconditional and irrevocable guarantee on the Notes:
- timely payment of interest (at any payment date); and
- ultimate payment of principal (at maturity).

Notes guaranteed by EIF have 0% RWA under CRD and Solvency II
EIF Portfolio Guarantee

EIF provides an unconditional and irrevocable guarantee on a loan portfolio:

- Risk retained by the Bank
- Risk covered by EIF as guarantor

Financial Intermediary

SMEs

The EIF guarantee may cover losses
- Pari passu with originator; or
- In the form of portfolio tranched cover

The EIF guarantee bears a 0% RWA under CRD and Solvency II
## Guarantee Instruments
### Development 2013 and beyond

<table>
<thead>
<tr>
<th>Product</th>
<th>Portfolio Tranche</th>
<th>Form</th>
<th>Leverage</th>
</tr>
</thead>
<tbody>
<tr>
<td>SME Guarantee Facility</td>
<td>First Loss</td>
<td>Direct guarantee Counter-guarantee</td>
<td>14</td>
</tr>
<tr>
<td>FLPG*</td>
<td>First Loss + Second Loss</td>
<td>Direct guarantee</td>
<td>5 to 7</td>
</tr>
<tr>
<td>Credit Enhancement</td>
<td>Second Loss (mezzanine)</td>
<td>Direct guarantee</td>
<td>6 to 8</td>
</tr>
<tr>
<td>RSI</td>
<td>Blended (uncapped)</td>
<td>Direct guarantee Counter-guarantee</td>
<td>5 (on EC FLP)</td>
</tr>
<tr>
<td>ABS wrap</td>
<td>Senior</td>
<td>Direct guarantee</td>
<td>2 to 3</td>
</tr>
</tbody>
</table>

* First Loss Portfolio Guarantee

Risk tolerance
Deal rationale
Financial Institutions
Pricing
Leverage
Self-sustainability
Target Beneficiaries
EIF catalytic impact

"Ex-ante assessment of the value added of the EIF guarantee
For each proposed operation, EIF measures the anticipated impact at market and transaction level, as well as the expected leverage / catalytic effect for the SME lending"

"Ex-post verification of the actual impact of the guarantee operation at final beneficiary level (SME)"

"EIF’s own risk guarantees
- supported more than 500,000 SMEs so far
- with cumulative guarantee commitments in excess of EUR 8 bn"
Richard Hopkin
Managing Director in the Securitisation Division, AFME
Association For Financial Markets in Europe

Re-starting the SME Credit Market in Europe: What role for securitisation and the capital markets?

9th April 2013
European Parliament, Brussels
European banks vs. rest of the world

**Eurozone bank assets:** €35tn

**Eurozone GDP:** €10tn

**Value of world’s gold stock:** €7tn

**US-Iraq war cost (2003-10):** €2.7tn

**Global hedge fund industry:** €1.6tn

**ESM:** €0.5tn

**Greek GDP:** €0.2tn

**Finding Nemo revenue:** €0.001tn

**Source:** RBS Credit Strategy, Bloomberg, Wikipedia
Deleveraging the banking system: €5.1tn needed

€5.1tn would get Europe to levels close to Australia or Japan, over the next 5 years

Total bank assets % GDP

Source: RBS Credit Strategy, ECB, IMF
Securitisation Primary Issuance (Placed)

European Placed Issuance

Sources: Bloomberg, Dealogic, Deutsche Bank, JP Morgan, Bank of America-Merrill Lynch, RBS, Thomson Reuters, UniCredit, AFME & SIFMA
Securitisation Placed Issuance by Collateral

Sources: Bloomberg, Dealogic, Deutsche Bank, JP Morgan, Bank of America-Merrill Lynch, RBS, Thomson Reuters, UniCredit, AFME & SIFMA
Securitisation Placed Issuance by Country

2011

- UK: 62%
- Netherlands: 15%
- Spain: 6%
- PanEurope: 1%
- Other: 2%
- France: 4%
- Germany: 8%
- Italy: 2%

2012

- UK: 58%
- Netherlands: 18%
- Spain: 1%
- PanEurope: 1%
- Other: 3%
- France: 9%
- Germany: 9%
- Italy: 0.4%

Sources: Bloomberg, Dealogic, Deutsche Bank, JP Morgan, Bank of America-Merrill Lynch, RBS, Thomson Reuters, UniCredit, AFME & SIFMA
2011 and 2012 SME issuance by jurisdiction (including retained transactions)

Source: Lloyds, ConceptABS
Placed SME securitisation by jurisdiction

- United Kingdom: 55%
- Germany: 13%
- The Netherlands: 14%
- Spain: 9%
- Italy: 9%

Source: Lloyds, ConceptABS
Historical Default Rates for Securitisation: Mid-2007 to End Q2 2012

<table>
<thead>
<tr>
<th>Original Issuance (EUR billion)</th>
<th>Default Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Europe</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Total PCS eligible asset classes</strong></td>
<td>957.8</td>
</tr>
<tr>
<td>Credit Cards</td>
<td>33.2</td>
</tr>
<tr>
<td>RMBS</td>
<td>753.0</td>
</tr>
<tr>
<td>Other consumer ABS</td>
<td>68.7</td>
</tr>
<tr>
<td>SMEs</td>
<td>103.0</td>
</tr>
</tbody>
</table>

| **Total Non-PCS eligible asset classes** | 736.8 | 4.06 |
| Leveraged loan CLOs              | 71.3  | 0.10 |
| Other ABS                        | 71.0  | 0.16 |
| Corporate Securitisations        | 67.7  | 0.33 |
| Synthetic Corporate CDOs         | 255.1 | 2.30 |
| CMBS                            | 165.2 | 4.55 |
| Other CDOs                       | 77.8  | 6.10 |
| CDOs of ABS                      | 28.9  | 39.44 |

| **Total European securitisation issuances** | 1,694.7 | 1.82 |
| **Covered Bonds**                  | 1,084.5 | 0.00 |

| **Total European issuances**       | 2,779.2 | 1.11 |

| **Select US asset classes**        |        |     |
| Credit cards                      | 295.4  | 0.00 |
| Autos                            | 198.2  | 0.04 |
| Student loans                     | 266.8  | 0.25 |
| RMBS                             | 3,255.0| 15.58 |

**Source:** Standard & Poor's
Historical Default Rates for Securitisation: Mid-2007 to End Q2 2012

Source: Standard & Poor’s, AFME
Historical Default Rates for Securitisation: Mid-2007 to End Q2 2012

Source: Standard & Poor’s, AFME
ABLe: an agency for business lending

- Requested by UK Department of Business, Innovation and Skills
- Stemmed from the Breedon Report
- Participants drawn from many fields of expertise
  - business and industry
  - accountancy
  - the law
  - academia and management consultancy
  - investors
  - banks
Areas of focus

- Eligible SMEs
- “Patient” finance: 5 years plus
- Existing hurdles
- Investors’ perspectives
- The impact on existing originators
- The role of government
The Agency for Business Lending

- A bridge to the capital markets
- Agnostic as to funding and risk transfer solutions
  - securitisation
  - covered bonds
  - sponsored funds, retail and investment
  - synthetic credit risk transfer
  - existing schemes
- Aligned with the Business Bank
- Leverage existing infrastructure
Delivering funding for growth with stability

- Tens of billions of Euros of funding is achievable, but this could be prevented by
  - excessive capital requirements
  - financial transaction tax
  - encumbrance restrictions
  - overlapping regulation
  - negative stereotyping
The Association for Financial Markets in Europe advocates stable, competitive and sustainable European financial markets, which support economic growth and benefit society.

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Unit SME access to finance, DG Enterprise and Industry, EU Commission
Restarting the SME credit market in Europe:
What role for securitisation and the capital markets?

Vilmos Budavari
DG Enterprise and Industry
Unit D.3 Access to Finance

• I would like to thank Miguel de La Mano (DG MARKT) for providing much of the material on which this presentation relies.

• The views expressed are my own and do not necessarily reflect those of DG ENTR or the European Commission. All errors are my own.

9 April 2013
Figure 1. Global yearly issuance by collateral - $ billion (Banque de France, Dealogic)

US Agency: Freddie Mac, Fannie Mae et Ginnie Mae

Données au 04/12/2012
Figure 2. European yearly issuance by country and collateral, $ billion (Banque de Fran
Deallogic)

Données au 04/12/2012

* Autres : Danemark, Autriche, Finlande, Hongrie, Chypre, Luxembourg, Rép. Tchêque, Slovénie, Bulgarie, Pologne, Lettonie

Source : Dealogic
What happened?
Structural flaws of securitisation

- *Misalignment of incentives*
- *Lack of transparency and complexity*
- *Over-reliance on ratings*
Figure 4. European Securitisation Issuance 2002 – 2010 € billion (Source: OCDE, AFME)
Focus on the SME loan securitisation markets

Evolution of SME loan securitisation in Europe (Source: EIF)
Collateral performance in Europe has remained strong in the past few years.

**Figure 9. European structured-finance default rates (mid-2007 to Q4 2010)**

Source: OCDE, Standard & Poor’s.

<table>
<thead>
<tr>
<th></th>
<th>ABS</th>
<th>Structured Credit</th>
<th>CMBS</th>
<th>RMBS</th>
<th>All European</th>
<th>All US structured finance*</th>
<th>All Corporate**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Values</td>
<td>0.16%</td>
<td>2.86%</td>
<td>2.74%</td>
<td>0.07%</td>
<td>0.95%</td>
<td>7.71%</td>
<td>6.34%</td>
</tr>
</tbody>
</table>

*by initial issuance volume

** by number of ratings
Bank deleveraging in Europe

Eurozone banking sector assets and GDP (AFME, Ernst & Young)
Measures addressing securitisation markets

- **Risk retention measures**
  - Risk retention rate in CRD II
  - Basel III requirements for re-securitisations

- **Transparency**
  - ABS loan-level initiative by the ECB
  - MIFID

- **New regulations on credit rating agencies**
Challenges remain in the short term

On the demand side
- Loss of investor's confidence
- Uncertain economic environment

On the supply side
- Impact of regulatory reforms

Competition from covered bonds
What are the key factors for securitisation markets to recover?

- Simplicity and transparency of structures
- Standardisation
- More placement of securitised products with investors
- Regulatory certainty
Green Paper on the long-term financing of the European economy

- The European Commission's recently adopted Green Paper on the "Long-Term Financing of the European Economy" puts forward ideas for the relaunching of securitisation markets.

- Stakeholders' opinion is sought on these by 25 June 2013.
Emmanouil Schizas

Senior Economic Analyst, ACCA
SME credit after CRDIV.
€650bn
Barclays’ estimate of EU banks’
deleveraging needs

5 yrs
Big 4 estimate of how long it will take

€2tn
IMF estimate of EU banks’
deleveraging needs

€6466bn
EU SMEs’ fixed capital
investment needs in 2012

The global body for professional accountants
ACCA
This is your bank on Basel.
Many channels of CRDIV feedback

- Higher costs of credit (spreads & fees)
- Tighter rationing of credit
- Leverage
- Change in business models
Figure 1. Historical development of the RWA/TA ratio of systemically important banks

$R^2 = 97\%$
### Table 1. Total loans to total assets: A historical perspective for selected banks (percentages)

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</tr>
</thead>
<tbody>
<tr>
<td>Deutsche Bank</td>
<td>85</td>
<td>73</td>
<td>53</td>
<td>17</td>
<td>11</td>
<td>15</td>
<td>21</td>
<td>27</td>
</tr>
<tr>
<td>UBS</td>
<td>78</td>
<td>61</td>
<td>26</td>
<td>15</td>
<td>18</td>
<td>21</td>
<td>27</td>
<td>22</td>
</tr>
<tr>
<td>BNP Paribas</td>
<td>77</td>
<td>73</td>
<td>37</td>
<td>28</td>
<td>31</td>
<td>28</td>
<td>36</td>
<td>38</td>
</tr>
<tr>
<td>Barclays</td>
<td>78</td>
<td>68</td>
<td>64</td>
<td>33</td>
<td>32</td>
<td>25</td>
<td>34</td>
<td>32</td>
</tr>
<tr>
<td>Bank of America</td>
<td>58</td>
<td>62</td>
<td>61</td>
<td>44</td>
<td>51</td>
<td>51</td>
<td>40</td>
<td>42</td>
</tr>
</tbody>
</table>
Goodbye SME loans, Hello SME credit?
£150m SME loan fund to shut to investors

By Mark Wembidge and Michael Stothard

A £150m fund intended to unlock finance for British small- and medium-sized enterprises struggling to obtain credit is to close to investors this week.

With thousands of small businesses squeezed by the dearth of bank funding, Palio Capital Partners hopes to provide an alternative with a fund providing a mix of senior debt, mezzanine debt and equity.

The scheme, targeting companies with an enterprise value of £10m-£100m, comes amid a withdrawal of lending to SMEs as regulation forces banks to shrink their loan books.

In March, a government report said the credit squeeze could lead to a funding shortfall for small British businesses of as much as £60bn by 2016.

Some 99.5 per cent of the 4.5m businesses in the UK are SMEs, according to government figures.

“What is shocking is the quality of the companies that have had capital withdrawn from them by the banks.”
Figure 21. Loan types that will be most difficult to divest

% of respondents who rated each of the following 4 or 5 (on a scale of 1-5, 5 = extremely difficult)

- Commercial real estate
- Corporate – other
- Retail – secured
- Small and medium enterprises
- Other
- Corporate – public sector
- Corporate – asset finance and leasing
- Retail – unsecured

% of respondents

The global body for professional accountants
INVESTISSEUR
Donnez du sens à votre argent

Taux de rémunération jusqu'à
4,50%

INVESTIR
A partir de 100€ / Capital garanti et rémunération nominale annuelle minimum garantie de 1%
Taux nominal annuel maximum de 4,50% au 15/03/2012
Selon la performance du panier de projets sélectionnés
Sur 3 ans / Capital récupérable à tout moment

ENTREPRENEUR
Obtenez un financement à visage humain

Financer un projet de 3.000€ à 25.000€
Indiquer le montant
Calculer la mensualité
Mensualité du prêt
Commission (unique)

DEPOSER SON PROJET
Pour obtenir un prêt bancaire pro de 3.000€ à 25.000€
(sous réserve d'acceptation bancaire et choix des investisseurs)
Sur 3 ans (commission : 4% du montant emprunté) au 15/03/2012
TEC : 11,36%

The global body for professional accountants
ACCA
The US precedent

- By 2009, nearly 2/3 of lenders originating SBA-backed loans relied on the secondary market for exits
- Fed could act as ‘buyer of last resort’
- Securitised SBA guaranteed loans were not seen as substantially safer in aggregation
The US precedent

- Hard to standardise business risk profile and demographics in these securities
- Some credit-relevant information missing
- Undermined the $15bn SME loan securities programme under TALF
Innovation, arbitrage, or fraud?
Information

- Securitisation economises on
  - Capital costs
  - Information production costs
- Cutting corners is not an economy
- What if we got someone else to…
On Monday, FT Alphaville reported on one significant consequence of the Dodd-Frank Act: rating agencies have had to ask their clients not to cite their opinions in prospectuses and registration statements.

The final version of the Dodd-Frank act amended an important provision of the Securities Act of 1933. That provision — Rule 436(g) — had essentially shielded rating agencies from so-called “expert liability”.

But since Dodd-Frank contained a provision that rescinded that rule, the rating agencies have found themselves in an awkward position. All three of the major agencies — S&P, Moody’s and Fitch — have issued statements that they are still working through the potential ramifications of the change.

And one market is already feeling the effects of the uncertainty, as RBS strategists Paul Jablansky and Brian Lancaster pointed out in a note on Tuesday (emphasis ours):

“**we believe that for the immediate future it will be difficult or impossible to bring new ABS, CMBS, and non-Agency MBS issues to the public market**; we also believe that, even with a longer-
IFR-ABS: Bill reversing rating agency liability advances

By Adam Tempkin
Wed Jul 20, 2011 1:39pm EDT

NEW YORK, July 20 (IFR) - The House Financial Services Committee on Wednesday voted to approve legislation introduced by Representative Steve Stivers (R-Ohio) that would repeal a provision of the Dodd-Frank legislation from last year which made credit rating agencies liable for increased lawsuit exposure.

The Asset-Backed Market Stabilization Act of 2011 (H.R. 1539), introduced early this year, would restore Rule 436(g) of The Securities Act of 1933, which exempted rating agencies from "expert" liability when they issue credit ratings on asset-backed securities.

The Dodd-Frank Act had repealed 436(g) and the ABS market froze in the summer of 2010 until the SEC issued a temporary no-action letter effectively exempting the rating agencies from liability.
Thanks!
Gerhard Huemer

Director Economy Policy, UEAPME
Q&As
Concluding remarks

Corien Wortmann-Kool, MEP

Cocktail reception