

## Results of our European securitisation investor survey: Let the sunshine in.

London, 15 June 2010, by Mike Nawas and Sharon Yeoh

As the European securitisation market gathers in London this week for the annual industry conference, many participants will be wondering if the market is finally showing signs of robust recovery and if perceptions towards securitisation are normalising. In this Market Insight, we share our findings from our survey of 26 investors. It provides insight into evolving attitudes, investment appetite and market prospects for the next 12 months. The consensus appears to be moving towards optimism; so, befitting a pre-summer conference, we signal a call to the market to “let the sunshine in”.

With the European financial markets once again locked in to pessimism since the Greek debt crisis, with concerns over sovereign debt spilling over to currencies, equities and credit, we believe that it is a good time to examine if the securitisation market stacks up positively or negatively against the overall backdrop. Initially, we decided to conduct a survey amongst a broad group of market participants into prevailing attitudes to securitisation with a view to understanding if existing concerns over rating migrations, market value declines and default rates were abating. As our research project progressed, it appeared that in particular the investor population was providing us with some striking conclusions. So we decided to focus this Market Insight on the feedback that we received from investment managers and investment advisers. We acknowledge that the sample size of 26 of these investors does not provide robustness in the scientific sense of the word but the outcomes do provide interesting insights in the extent to which investors believe that securitisations are weathering the storm.

We conducted our survey in the first weeks of June, so well after the Greek debt crisis had taken its toll over the volatility, CDS spreads and new issue volumes of all credit asset classes. It appears that notwithstanding the currently low level of market activity, there is a striking positive

consensus on the prospects of the European securitisation market for the next 12 months. Whilst pre-sold and privately placed deals continue to dominate the European securitisation market, driven by caution on the part of issuers and arrangers, there appears to be – at least as far as the buy side is concerned – not such a need for this cautionary stance, boding well for prospects of further recovery of the public ABS markets.

We draw three main conclusions:

First, European securitisation still suffers from a general tainting by association with the poor performance of some securitisation asset classes. Second, nevertheless and even after the recent market volatility in sovereign debt and equities, European ABS investors remain broadly optimistic on the market for the next 12 months.

Third, especially for the AAA rated segment of the market, this optimism appears to be fundamental, i.e., emanating from a robust appetite.

Let us examine the conclusions in greater detail.

### **General tainting**

One might have expected that because the securitisation market is highly technical in nature, general investor perceptions would be driven by

technical risk analysis rather than by macro concerns over the quality of assigned ratings and the robustness of securitisation as an investment proposition per se. It appears, however, that the general aversion towards securitisation as a whole, notwithstanding vast differences in investment performance between asset classes, remains pervasive: 65% of investors believe that securitisation as a general investment proposition has truly been damaged by the credit crisis. So the crisis was not a storm in a teacup and the basic attitude towards this market is still suffering from the traumatic events that were caused by a number of sub-markets of securitisation. The persistence of the general negativity is surprising, especially as when we dug deeper and asked our respondents to confirm the “true damage” per asset class, the results appeared to be quite different: a meagre 16% believed that true damage was done to Prime RMBS or Auto ABS. And if you consider that well over 60% of European market consisted of exactly those asset classes (Source: AFME/ESF), and, in addition, that our respondents generally seem to believe that losses on their investments were mainly due to market repricing rather than credit impairments, one would have expected that the general tainting by CDOs or US subprime deals would have waned by now. Not so, as yet.

Qualitative feedback from the interviews, however, does lead us to predict that as time goes by and the underlying credit performance of the vast majority of securitisation transactions remains strong, this general tainting will fade as the focus of concern shifts elsewhere. As one investor put it pointedly: “let’s not forget that even now credit spreads for many ABS asset classes are tighter than for some European sovereigns”.

### **Optimism for the next 12 months**

We asked our respondents to predict the market for the next 12 months in two aspects: volume of new issuance and spread movement. In both ways, our investors displayed optimism. An over-

whelming 62% believes that new issue volumes in the next 12 months will be higher than in the last 12 months, while at the same time over 80% believes that those new issues will be absorbed with stable or even tightening credit spreads. Only 19% of respondents believe that spreads will widen from here.

We find the spread forecast by our respondents quite punchy, given that spreads have already come down markedly across the board over the last year. In the monthly data report provided by Markit for AFME/ESF the 3-5 year AAA European RMBS spread range has moved in the last 12 months from 350-650 bps to 120-280 bps. Further tightening would bring us back to levels last seen before the Lehman collapse in 2008.

As far as the volume prediction is concerned, we find our respondents’ views less surprising. In today’s market, where the vast majority of new issuance is retained by banks for ECB repo purposes (in 2009, 94% of the total new issuance volume of €414 Billion where retained by banks, according to AFME/ESF) volume predictions depend on one’s definition of “volume of new issuance”. And because we canvassed investment managers and investment advisers, who are only able to purchase the non-retained deals (€25 Billion in 2009), we expect that when they answered our question, they focused on those non-retained deals. The qualitative feedback underscored this view, as we found that generally investors are expecting to see more bonds come their way over the next 12 months.

### **Fundamental appetite**

The optimism that we detected amongst respondents seems largely driven by fundamental appetite rather than tactical considerations. Especially in the AAA rated segment, investors seem re-committed to the market: 57% of investors disagree with the statement that their “appetite for AAA rated European securitisations has deteriorated permanently”. We do caveat, however, that although the respondents may feel

that their appetite has not deteriorated permanently, probably overall the appetite has decreased because there simply are far less investors active in the AAA segment, mainly due to the demise of SIVs.

Investors feel no strong need to have a US style TALF programme to support their willingness to engage in the European ABS market. Moreover, this willingness pertains to both primary and secondary markets. Interestingly, when forced to choose between relative value in secondary versus more thinly priced but firmly untainted deals in primary, only a minority (31%) of our respondents opts for the fresh deals. This boldness appears not to be derived from an unshaken belief in a strong correlation between the robustness of ABS structures and the ultimate return on investment, as only a 35% minority of respondents actually believe in such a correlation. Rather, since the crisis, they increasingly acknowledge the need to do their own credit work anyway when making investment decisions. If that is the case, one might as well opt for relative value, be it in secondary or primary.

## Conclusion

We re-iterate that our sample size warrants caution. However, the survey results and qualitative feedback provide a striking sense of optimism that we wish to share with our readers. Issuers may be well advised to consider tapping in to this optimism over the next 12 months, as investment appetite may be surprisingly robust for European securitisations, notwithstanding persistent difficulties in other fixed income instruments such as European sovereign bonds. This should be good news for the market gathered in London for their pre-summer conference. Let the Sunshine In.

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## Overview of questions and responses:

1. ABS as an investment proposition has truly been damaged through the credit crisis; it was not a storm in a teacup.
2. For each of: European Prime RMBS  
European CMBS  
European Bank CLOs  
European Auto ABS
3. I think the European authorities should implement a US TALF style programme to support the European ABS market.
4. In general, since the crisis, European ABS investors have suffered market risk losses rather than real credit impairment losses.
5. The structural robustness of ABS makes its ROI more predictable than for unsecured corporate bond investments with comparable credit ratings.
6. My investment appetite for AAA rated ABS has deteriorated permanently as a result of the credit crisis.
7. The same for BBB.
8. Notwithstanding the relative value that may exist in legacy ABS, I prefer newly issued, newly rated ABS with fresh collateral.
9. For the next 12 months, I expect ABS credit spreads to [ ]
10. I expect new issue volumes of ABS in the next 12 months to be [ ] than in the last 12 months.

Average Score	Number of responses	1 - Totally disagree	2 - Disagree	3 - Neutral	4 - Agree	5 - Totally agree
3.7	26	0%	23%	12%	42%	23%
2.6	26	8%	46%	31%	8%	8%
4.2	26	0%	4%	15%	38%	42%
3.8	26	4%	15%	19%	23%	38%
2.5	25	8%	60%	16%	8%	8%
2.7	26	15%	38%	15%	23%	8%
3.6	26	4%	19%	4%	58%	15%
2.8	26	8%	46%	12%	27%	8%
2.8	26	19%	38%	4%	23%	15%
3.4	26	4%	23%	19%	35%	19%
2.8	26	8%	46%	15%	19%	12%
		<b>6 - widen</b>	<b>7 - tighten</b>	<b>8 - stay the same</b>		
	26	19%	50%	31%		
	26	62%	15%	23%		