Securitisation of Debts

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Introduction

The financial system all over the world is in transforming stage. The capital, money and debt markets are getting widened and deepened. The development of debt market increases the efficiency of capital market. The debt or assets securitisation plays very important role. It is the debt market which has provided more impetus for capital formation than equity market in the economically advance countries.

In the coming chapter we are going to learn about yet another but very new in nature debt instrument, known as **“SECURITISATION”**.

Meaning, Definition

The securitisation of debt or asset refers to the process of liquidating the long term assets like loans and receivables of financial institutions by issuing marketable securities against them.

The definition can be stated as, “A carefully structured process whereby loans and other receivables are packaged, underwritten and sold in the form of asset backed securities”.

Structured Securities Vs Conventional Securities

Securitisation is basically a structured financial transaction. It is very much different from conventional securities like bonds, debentures etc. on following points.

a] Source of repayment

b] Structure

c] Nature

Securitisation Vs Factoring

The Securitisation is also differs from Factoring, on following points :

Securitisation	Factoring
Associated with Assets.	Associated with Book Debts.
Deals with Loans.	Deals with Bills Receivables.
Nature is Medium or Long.	Nature is short term.
Collection work is done by originator or agency.	Collection work is done by factor himself.
Part of credit risk is cab be absorbed by originator.	Whole credit risk is on the shoulder of factor.

Modus Operandi

In securitisation following parties are required;

a] The originator

b] A Special Purpose Vehicle (SPV) or trust

c] A merchant or investment banker

d] A credit rating agency

e] A servicing agent-Receiving & Paying agent (RPA)

f] The original borrowers or obligors.

g] The prospective investors i.e. the buyer of securities.

Stages in Securitisation

There are five stages involved in the working of Securitisation

A] Identification stage / process

B] Transfer stage / process

C] Issue stage / process

D] Redemption stage / process

E] Credit Rating stage / process

Types of Securities

As stated earlier, securitisation is liquidating long term assets in to marketable securities, the asset's quality, amount of amortisation, default experience of original borrower, financial reputation and soundness etc. is vital.

There are three important types of securities;

a] Pass through and pay through certificates
b] Preferred stock certificates
c] Asset based commercial paper.

Securitisable Assets

After seeing the types of assets, it is good to see that which type of assets are securities. Because generally securitisation is not suitable to trade debts & receivables because they are readily accepted by factor. Following are different assets which are generally securities.

a] Term loan to financially reputed companies.
b] Receivables from Government Department.
c] Credit card receivables.
d] Hire Purchase loan like vehicle loan.
e] Lease Finance.
f] Mortgage loans.

Advantages of Securitisation

Securitisation provides benefits to all the parties, such as, the originator, investor and the regulatory authorities. Some of them are as below;

a] Additional Source of Fund

b] Greater Profitability

c] Enhancement of Capital Adequacy Ratio

d] Spreading of Credit Risk

e] Lower Cost of Funding

f] Provision of Multiple Instrument

g] Higher Rate of Return

h] Prevention of Idle Capital

i] Better than Traditional Instrument

Why Banks Should Enter in Securitisation

After seeing the advantages of Securitisation, it is quite clear that if this type of venture get rooted in Indian soil it will definitely boost our economy to great extent.Commercial banks play vital role in this because of following points.

a] Innovative and Low Cost Source of Fund

b] Better Capital Adequacy Norms

c] Creation of More Credit

d] Increased Profitability

e] Tool for Asset-Liability Management

Conditions for Successful Securitisation

Every business will prosper only when it is done with some code of conduct or conditions. Securitisation also have no escape. Below mention conditions are must for achieving successfulness in securitisation.

a] Ability of original borrower to repay

b] Scientific Credit Rating System

c] The SPV should be separate organisation

d] Instruments arising out of securitisation should be listed in Stock Exchange

e] Two way quotation systems, as like Mutual Fund

f] Standardised loan documentation system

g] Proper Accounting System

h] Adequate Guidelines should be given by authorities

Securitisation Abroad

The credit of starting securitisation goes to America, where the first structured asset securitised financing came into being in 1970. Although firstly it was backed by mortgage loans. The securities issued by it were called "Mortgage pass through securities". However in 1985 non mortgage collaterals started getting securitised in U.S.A.

Securitisation is gaining popularity in UK also in recent years. Like America the concept firstly backed by mortgage.

Securitisation of debt and the consequent debt instruments are now popular in countries like Italy, Australia, Canada Japan, France etc.

Securitisation in India

In India the concept of securitisation is still new. In Feb. 1991, the securitisation of ICICI’s receivables by Citibank was the first attempt. A sum of Rs. 15 crores was raised. The Hire purchase portfolio of TELCO was securitised by Citibank. Infact the securitisation was pioneered in India by Citibank. Now HDFC is on the way to securitised its housing loan portfolio through Citibank. If securitisation has to become popular in India, the commercial bank should enter in this field in big way. By doing this, commercial bank can remove their non performing assets from their balance sheet.

Causes of Unpopularity in India

Till now we seen lots of advantages of securitisation and benefits, but in India it is not firmly rooted because of ;

a] New Concept
b] Heavy Stamp Duty
c] Cumbersome Transfer Procedure
d] Difficulty in Assignment of Debt
f] Absence of Standardised loan Documentation
g] Inadequate Credit Rating System
h] Absence of Proper Accounting Systems
i] Absence of Guidelines

Future of Securitisation in India

The future of securitisation in India is still very bright due to following points,

a] Liberalisation of financial markets
b] Growth of capital market & increase in the investors
c] Entry of financial instruments like Mutual Funds
d] Popularity of debt instrument
e] The proposal by Narsimhan Committee.

In India the scope for securitisation is very high in case of loans like Mortgage, housing loans, other term loans etc.