

# ASJ

## AUSTRALIAN SECURITISATION JOURNAL

Incorporating Australian  
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>> Issue 08 • 2015

## Under scrutiny

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### PRS 11

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### PRS 13

Deal Size - **A\$400m**  
Date Issued - Oct 2014

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# FROM THE FEDERAL ASSISTANT TREASURER

I am pleased to have the opportunity to provide the foreword for this issue of the ASJ. Since taking on the role of assistant treasurer, I have welcomed the opportunity to meet with representatives from across Australia's financial-services sector, and value the contribution of bodies such as the Australian Securitisation Forum (ASF) in promoting and representing the industry to government and policymakers.

Australia has a strong and robust financial-services sector that has served us very well, supporting economic growth and making a direct contribution to the nation's finances. The financial-services sector represents around 9 per cent of the Australian economy, and employs around 413,000 people. In addition to its direct economic contribution, the sector supports the

*«Securitisation is an important part of Australia's financial system, and plays a vital role in promoting competition in the lending market by providing funding for many smaller banks and nonbank lenders, as well as allowing larger banks to diversify their funding sources.»*

growth of the Australian economy through its role in facilitating savings and investment.

Securitisation is an important part of Australia's financial system, and plays a vital role in promoting competition in the lending market by providing funding

for many smaller banks and nonbank lenders, as well as allowing larger banks to diversify their funding sources.

The Australian securitisation market has continued to strengthen. In 2014, we saw about A\$33 billion (US\$26.5 billion) of asset-backed securities issued into the market, which was an increase of around A\$1 billion from the previous year. This trend has continued into 2015, with around A\$12 billion of issuance so far.

The government is currently considering its response to the final report of the Murray Inquiry into the financial system. The inquiry has made a comprehensive range of recommendations to strengthen the operation of Australia's financial system. I thank the ASF and its members for their positive contribution to this important inquiry.

The Australian Prudential Regulation Authority (APRA) is reviewing the prudential rules governing securitisation in Australia. I encourage the industry to continue its engagement with APRA in developing a set of rules that strike the right balance between stability and efficiency in the market.

I look forward to continuing to work with the ASF and the industry as a whole, in the interests of building a more efficient, stronger and successful Australian financial system.



**THE HON. JOSH FRYDENBERG MP**  
ASSISTANT TREASURER, AUSTRALIA

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# FROM THE CHIEF EXECUTIVE

**W**elcome to the mid-year edition of ASJ. As things stand, 2015 will be a pivotal year for the Australian securitisation market. Primary-market activity for both residential mortgage-backed securities (RMBS) and asset-backed securities (ABS) in the first six months has been the strongest since the financial crisis.

New issues have typically been oversubscribed with a mixture of financial-institution and real-money investors. With record low interest rates there has been, in particular, strong interest in the higher-yielding subordinated tranches of new issues. An increased frequency of new issues and strong investor interest are positive markers for the market.

We expect the second half of 2015 to see several major developments that will influence the outlook of the market.

The new Reserve Bank of Australia (RBA) repo-eligibility criteria for RMBS and ABS come into effect from July. The new rules require issuers of RMBS or ABS to provide an expanded and more standardised set of information to the RBA and other qualified market participants. RMBS issuers wishing to ensure their securities are repo eligible with the central bank will need to provide detailed loan-level information. Preparation for providing the loan-level data has been under way for more than 12 months and represents a substantial investment by issuers in the future of the market.

Another significant development anticipated in the second half of 2015 is the release of the final draft of the new prudential standard governing the multiple roles played by Australia's regulated financial institutions as issuers, investors or transaction counterparties in RMBS and ABS. The regulator – the Australian Prudential Regulation Authority – has flagged its objective of providing a prudential framework that supports a large and simple securitisation market.

The industry is keen for the standard to facilitate efficient transaction structures that permit issues of securities with term and currency characteristics appealing to both local and international investors.

A third major development to affect the securitisation market in late 2015 and beyond will be the commencement of a divestment programme by the Australian Office of Financial Management (AOFM) of the RMBS portfolio it acquired between 2008 and 2012. The AOFM has communicated that it is mindful of the potential for the divestment programme to affect the RMBS market. Subject to market conditions, the AOFM expects to sell A\$300-500 million (US\$240.5-400.9 million) of RMBS per calendar month. As at the end of May the AOFM's holdings in RMBS were circa A\$4.6 billion, in amortised face-value terms. The AOFM planned to conduct the first monthly auction in June 2015.

Finally, the ASF national committee met to discuss its business plan and budget for the 2016 membership year. The main focus will remain on its core and long-standing objectives. These are primarily to provide the Australian market with a platform to discuss market and regulatory matters, advocate on behalf of members, provide a comprehensive suite of professional-development programmes, improve market standards and practices and promote the market to global investors and policy makers.

I look forward to an exciting period leading up to the ASF's annual conference, which starts on November 30 at the Sydney Hilton.



A handwritten signature in black ink that reads "Chris Dalton". The signature is written in a cursive, flowing style.

**CHRIS DALTON**  
CEO, AUSTRALIAN SECURITISATION FORUM

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# THE ASF PERSPECTIVE

The **Australian Securitisation Forum (ASF)** is pleased to once again present an overview of its advocacy, outreach and education mission over the past six months, and offer an insight into where future activity will likely be focused.

BY **ALEX SELL**, CHIEF OPERATING OFFICER, ASF

**T**he ASF has focused on two key matters in the first half of 2015. The first is Reserve Bank of Australia (RBA) eligible-collateral reporting arrangements for residential mortgage-backed securities (RMBS). The second is engagement with the prudential regulator, the Australian Prudential Regulation Authority (APRA), in a bid to refine the Australian master trust so that it satisfies prudential as well as investor expectations.

We also saw, in the government's 2015 budget, an instruction to the Australian Office of Financial Management (AOFM) to sell down its holdings of RMBS. It had invested in this portfolio during the three phases of its post-financial-crisis cornerstone investor function. More on that later in this column and, in the form of market views, on p38 of this edition of *ASFJ*.

## RBA REPORTING – A NEW STANDARD FOR THE INDUSTRY

As Australian readers will know, the RBA will provide contractual cash liquidity to 13 of Australia's largest banks in

order to meet the shortfall in their liquidity coverage ratios set by APRA, arising because of the lack of qualifying high-quality liquid assets on issue.

In return for this cash liquidity, banks that have entered in to the contractually binding committed liquidity facility (CLF) will pledge repo-eligible collateral. Where this collateral is in securitised form, public reporting on the collateral's composition will be required following each coupon distribution.

The ASF has worked with the RBA to resolve or clarify both definitional and technical aspects of the new reporting requirements. It is estimated that several million dollars has been spent by the industry to prepare for the new, more comprehensive and standardised information to be reported for both RMBS and asset-backed securities that seek to be repo-eligible with the RBA.

The ASF has funded the drafting of a nondisclosure agreement for the exclusive use of ASF members, in an attempt to streamline and standardise the contractual basis upon which data will be secured, used, and accessed. This will serve as the backbone of agreements between sponsors and their investors.

## RESEARCH LIBRARY

We have added new material to our online research library, with plenty more to come. The library provides domestic and international visitors with articles providing background on the nature, structure and performance of the Australian securitisation market and the underwriting of financial assets funded through securitisation.

## AOFM UPDATE

In the 2015 federal budget, Australia's federal treasurer directed the AOFM to divest the Australian government's investments in RMBS. The treasurer's direction cautions the AOFM to be "mindful of the potential for the divestment programme to [affect] the RMBS market". It adds that "subject to market conditions, the AOFM [should] sell A\$300-500 million [US\$240.5-400.9 million] of RMBS per calendar month – based on the total amortised face value of notes to be sold, which will exclude accrued interest, gains on disposal and repaid capital". As of May this year, the AOFM's holdings in RMBS are circa A\$4.6 billion in amortised face-value terms.

While consensus is that this is unlikely to have a material impact on the market, there are concerns at the margin that the impact on fundamental demand and supply – particularly of non-major-bank securitisation, which of course was the programme's *raison d'être* – may be unhelpful in terms of repricing future funding costs.

## OFFSHORE INITIATIVES

The perennial round of global outreach efforts in London, Las Vegas, Barcelona, Tokyo and Singapore will be maintained,



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with Auckland recently added to the list. This outreach has been valuable and has led to mandates being secured.

What we have confirmed is the easily overlooked, but ultimately unavoidable, reality that investors – not only between nations but also within sectors – differ significantly in their outlook, preparedness, and relative-value perspectives. Accordingly, there is no one-size-fits-all strategy being adopted by the ASF, and we very much appreciate the financial and local support given by Austrade and our members.

## ASF ANNUAL STRATEGY REVIEW

With a renewed National Committee, the ASF has conducted some fresh thinking on how best to deliver on the its troika mission – education, consensus and advocacy. All three were all found to be performing well. In summary:

- ◆ Professional development needs for the industry were endorsed so that the core offering remains. Based on market feedback, a slimmed-down version of our advanced-level programme will be offered with the addition of relative-value content. Securitisation Fundamentals Online has only seen limited take up, so a reduction in its price will seek to increase its appeal.

- ◆ Policy and advocacy work were felt to be effectively managed, with no significant change in positioning or resources required. A re-proposed APS120 is expected to attract most of our policy focus over the next 12 months.

- ◆ Communications-related activity, including the ASF conference, evening series, ASF website, investor outreach and newsletter were all acknowledged as delivering valuable content to members and broader stakeholders, although costs need to be contained.

## NEW AUSTRALIAN PRUDENTIAL STANDARD

At the time of writing we, like the rest of industry, continue to wait with baited breath to read APRA's revised APS120, due for release later this year. Of particular interest will be how APRA wishes to see Australian master trusts operate in practice, having this year endorsed their use in principle.

## G20 OTC REFORM

Success was ours in securing the agreement of the Australian Securities and Investments Commission and government to not oblige securitisation special-purpose vehicles (SPVs) to report their OTC exposures.

We argued that not only were SPVs incapable of doing this under their trust deeds – although awkward delegations could in principle be produced – but that so-called 'single-sided' reporting would not undermine the motivation for the rules. Swap providers – as the major swap counterparties – report the position to the trade repository regardless. All that would occur would be duplication for no prudential benefit. There were other arguments, such as the fact that these SPVs are not systemically significant and face collateralised swap counterparties.

**“What we have confirmed is the easily overlooked but ultimately unavoidable reality that investors – not only within sectors but also between nations – differ significantly in their outlook, preparedness, and relative value perspectives. Accordingly, there is no one-size-fits-all strategy being adopted by the ASF.”**

However, the second phase of the reform is posing a threat to the very essence of securitisation. Margining and collateral requirements from the reforms could potentially cripple securitisation SPVs because credit-rating analysis relies upon a closed pool of collateral for the exclusive benefit of noteholders.

**“At the time of writing we, like the rest of industry, continue to wait with baited breath to read APRA's revised APS120, due for release later this year. Of particular interest will be how APRA wishes to see Australian master trusts operate in practice, having this year endorsed their use in principle.”**

SPVs are inert entities without a body corpus and only have collateral in the pool for the benefit of noteholders, not for the benefit of meeting unknown and uncertain amounts for swap providers. More to the point, swap providers are already fully collateralised because they are senior in the cash-flow waterfall and hierarchy of creditors, and

only have to hedge whatever cash flows pass through the trust. In other words, the trajectory of the regulation was trying to solve a problem that does not exist in relation to securitisation SPVs.

It seems this is a global issue. The ASF has reached out to its European and US colleagues who are facing identical concerns amid a regulatory resolve to deliver on G20 commitments without appreciating the nuances posed by securitisation vehicles. The ASF has formally asked the International Organization of Securities Commissions to revisit the scope of these reforms. ■

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# ADVANCEMENT FORUM

**T**he Australian Securitisation Forum's Women in Securitisation subcommittee, chaired by Resimac's head of capital markets, **Mary Ploughman**, seeks to provide women in the securitisation industry with high-quality networking opportunities, raise awareness of issues that affect their professional advancement,

and encourage engagement from different levels of seniority. On April 15, ANZ hosted the latest Women in Securitisation networking lunch at its Sydney offices. The lunch also featured a presentation and Q&A session with **Andrew Géczy**, chief executive officer, international and institutional banking at ANZ.



*“We know we get manifestly better decision making when we have more diverse people. You will have better business performance and outcomes if you have better diversity within a business – diversity in gender but also of thought process, which comes with cultural diversity.”*

ANDREW GÉCZY



*“I’m a passionate believer that we all need to strive for balance in our lives. We have to choose the dimensions of life which are important to us, and every once in a while reflect on them and decide which dimension will take a priority – this is something which often people don’t make conscious decisions about. You can’t succeed in human endeavour in the long term without life balance.”*

ANDREW GÉCZY



*“This is the seventh Women in Securitisation event and each time the energy and number of people interested grows larger. People are very keen to engage and to connect with others in the industry, and I hope this momentum builds further in the future.”*

MARY PLOUGHMAN



The Australian Securitisation Forum is pleased to announce its first-ever industry-wide Women in Securitisation lunch.

The event is open to all members of the ASF's Women in Securitisation group.

**When:** Tuesday 20 October

**Where:** The Establishment Ballroom, Level 2, 252 George Street, Sydney

**Time:** 12.00-2.00pm

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**Keynote speaker:**

GRETEL KILLEEN

*Journalist, author and media personality*

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For further details, please contact the ASF by emailing [asf@securitisation.com.au](mailto:asf@securitisation.com.au)



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# INCREASED SCRUTINY

*Australian mortgage lending standards have been brought back into the spotlight since the Australian Prudential Regulation Authority (APRA) began undertaking a review in response to circumstances which make the housing market an economic concern. Securitisation market participants say the sound underwriting standards which characterised Australia through the crisis remain in place – and that local asset-backed product maintains its gold standard.*

BY SAMANTHA MENZIES

In December last year, APRA wrote to authorised deposit-taking institutions (ADIs) outlining plans to further reinforce sound lending practices and mitigate any speculative pressures which may be building in Australia's housing market. The regulator pointed to historically low interest rates, high household leverage, the concentration of housing loans on ADI balance sheets and competition in the housing market as reasons for its focus.

APRA has played its cards close to its chest in terms of the conclusions it has so far drawn from its review. The regulator has made two key public pronouncements on the issue which, taken together, suggest it does not have systemic concerns but has uncovered some selective tweaks it will expect to be undertaken (see box on p14).

By mid-May, the APRA review process was ongoing. Due to issues of confidentiality around the review itself, lenders and other market participants were understandably reluctant to comment directly on the development.

However, in general terms bank lenders say they have a positive outlook on the review, arguing that any negative connotations – the tweaks APRA asks ADIs to make to their lending criteria – should be outweighed by the *de facto* seal of approval a completed review will give the sector.

Even nonbank lenders, which are not regulated by APRA and thus do not fall under its review, are optimistic that the outcome will benefit Australia's mortgage industry as a whole.

Some point out that the move could incentivise all issuers' lending standards to meet a certain level. Others back their own credit criteria, suggesting a bigger opportunity for nonbanks should increase market diversity and dilute some of the lender concentration seen through, and after, the financial crisis.

## COMBINED EFFORT

It is not just APRA which is paying close attention to mortgage lending in Australia. Indeed, its review was likely spurred at least in part by suggestions made by the Reserve Bank of Australia (RBA) as a consequence of the reserve bank's concern that the local housing market is growing out of sync with the rest of the economy.

In fact, the moves made by both APRA and the RBA represent a combined regulatory effort to reinforce Australia's sound residential mortgage-lending practices. APRA's December 2014 letter to ADIs confirms that its steps to review lending practices "have been developed following discussions with other members of the Council of Financial Regulators". These comprise APRA, the RBA, Treasury and the Australian Securities and Investments Commission.

The RBA has made it clear across a number of monetary policy statements that residential property prices are a concern, as inflation in the sector races ahead of sluggish growth elsewhere in Australia. However, the reserve bank has also been reluctant to take specific steps itself: instead, late last year the RBA flagged its preference for macroprudential-type tools to be used by the prudential supervisor.

Macroprudential tools, such as restrictions on the quantity of high loan-to-value ratio (LVR) home loans banks can write, have been used in other countries to cool down property-sector booms without adversely affecting the economic recovery elsewhere (see p20).

The RBA also has a specific prudential interest in Australian mortgages, as residential mortgage-backed securities (RMBS) form a substantial part of most large ADIs' liquidity books – meaning the asset class could expect to be offered for repo in large volumes should Australian banks face a future liquidity crisis. In late 2012, the RBA announced new repo-eligibility criteria for RMBS to aid its own information flow on the assets (see box on p18).

## AUSTRALIA STACKS UP

Australian market participants have traditionally trumpeted the sound lending standards which underpin local securitisation. The key fact they point to is that the disruption of the financial crisis in Australia did not entail credit issues with asset-backed product.

Rating agencies acknowledge the consistent performance of Australian RMBS. Vera Chaplin, managing director, structured finance ratings Asia Pacific at Standard & Poor's Ratings Services (S&P) in Melbourne, says: "When the financial crisis hit, the shock didn't affect the Australian economy

as severely as in the US and other western economies, and the performance of Australian residential mortgages only deteriorated moderately.”

She adds: “Subprime and low-doc loan borrowers were more

affected, particularly those in the 2004-06 vintages of lending. This was to some extent evidence of credit expansion and lending standards beginning to loosen in the period of cheap credit leading up to the financial crisis. Although the Australian economy remained relatively strong following the onset of the crisis, borrowers became more cautious. This in part drove down retail spending, which wasn’t great for the economy but was positive in terms of credit quality.”

Chaplin highlights the fact that the Australian market did not develop a very low-quality mortgage product. “Australia has never had the US-style segregations which created sizable market penetration for products like alter-A, jumbo loans and subprime lending. The Australian products have been predominantly prime, with a very small presence of non-prime products, and lending practices have generally been fairly uniform. This has meant that, systematically, Australia has less exposure to the contagion effect of a US-style subprime crisis,” she says.

In this context, efforts elsewhere in the world to bolster lending standards can be viewed as levelling the playing field relative to Australia rather than taking steps ahead. Jennifer Wu, Sydney-based senior credit officer, structured-finance group at Moody’s Investors Service (Moody’s), suggests that while Australia retains high-quality lending standards these may no longer outdo other jurisdictions. Again, economic conditions provide much of the risk.

“The lending environment has changed globally since the financial crisis,” Wu tells ASJ. “In the US and Europe there has been some tightening of lending criteria. As a result, in the current Australian environment of high house prices, interest-rate cuts and housing-market competition, I’m not sure claims that Australian mortgage lending is of a higher quality than elsewhere are still as true as they were a few years ago.”

## ECONOMIC BACKDROP

As APRA suggests, the real reason for the renewed scrutiny of Australian mortgage lending on the part of regulators is the economic backdrop. In May, the RBA cut interest rates by 25 basis points to 2.00 per cent – its second cut

*“People do not sell their house just because its value goes down – a home loan is not like a margin loan. As long as you continue making your mortgage payments the bank isn’t going to come knocking on your door.”*

**GUY VOLPICELLA** WESTPAC BANKING CORPORATION



in 2015. The reserve bank itself acknowledges that while lower interest rates are prudent for the Australian economy as a whole, the housing market is an outlier.

“Growth in lending to the housing market has been steady over recent months. Dwelling prices continue to rise strongly in Sydney, though trends have been more varied in a number of other cities,” the RBA’s May monetary-policy statement says. “The [RBA] is working with other regulators to assess and contain risks that may arise from the housing market.”

Following the May interest-rate decision, Fitch Ratings (Fitch) commented that this rate cut is likely to further fuel Australian house prices, particularly in Sydney, at a time when the authorities are trying to take the steam out of the market.

In a post-rate-decision report, the rating agency pointed out that strengths supporting the Australian economy as a whole could be “undermined by further increases in property prices and household debt, given mortgages form the largest asset class for Australian banks”.

Indeed, some analysts argue that the May cut might simultaneously add even more impetus to the housing market while largely failing to stimulate other sectors. Annette Beacher, head of Asia-Pacific research at TD Securities (TD) in Singapore, writes that the May cut is “not only a waste of a bullet, it has the potential to merely exacerbate the existing imbalances in the economy, ie hot housing and record levels of household debt, while exports – mining and non-mining – push up against an overvalued exchange rate”.

As APRA pointed out when it first announced plans to review Australia’s mortgage-lending practices late last year, historically low interest rates, high household leverage, ADI balance-sheet concentration on housing loans and competition in the housing market are concerns for the future of the mortgage and housing markets.

After a long period in the 5-6 per cent range, Australia’s unemployment rate exceeded the 6 per cent mark in mid-2014

*“We expect unemployment to go up and we think the rebalancing of the Australian economy could be slower than the market would like it to be, but unemployment is not likely to go up rapidly and cause a major collapse.”*

**VERA CHAPLIN** STANDARD & POOR’S RATINGS SERVICES



## APRA takes a long hard look

BY LATE MAY, THE AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY (APRA)'S CHAIRMAN HAD PUBLICLY SPOKEN TWICE ABOUT ITS REVIEW OF MORTGAGE-LENDING STANDARDS. THE FIRST PRONOUNCEMENT SUGGESTED APRA SEES NO SYSTEMIC PROBLEMS, WHILE THE SECOND IDENTIFIED A NUMBER OF SPECIFIC ISSUES TO BE ADDRESSED.

In an appearance before Australia's Senate Economics Committee in Canberra on February 25 this year, APRA's Sydney-based chairman, Wayne Byres, stressed that the regulator's main goal is to ensure the housing market evolves while housing finance remains sensibly founded on sound lending standards.

As a whole, Byres implied during his Senate appearance that the regulator believes the Australian banking system's lending standards are sound. APRA has requested that banks' investor-lending portfolios grow at no more than 10 per cent annually – a limit, Byres noted, achieved on a system-wide basis. "Many lenders were already using serviceability measures which were at or above benchmarks we set," he said.

In the APRA chairman's latest speech, delivered on May 13, the regulator offered its first public insight into the review. By contrast, this gave the impression that APRA is far from universally happy with the way all authorised deposit-taking institutions (ADIs) calculate borrowers' likely ability to service mortgage debt.

### TEST RESULTS

Byres disclosed significant detail around one specific test to which APRA subjected a number of "larger housing lenders" as part of the review of mortgage-lending standards the regulator initiated in December last year. The test required lenders to submit their serviceability assessments for four

hypothetical borrowers: two owner-occupiers and two property investors.

"The outcomes for these hypothetical borrowers helped to put the spotlight on differences in credit assessments and lending standards. The outcomes were quite enlightening for us – and, to be frank, a little disconcerting in places," Byres told the Customer-Owned Banking Association (COBA)'s CEO and Director Forum in Sydney.

APRA discovered that mortgage lenders' assessments of borrower risk feature "wide differences", resulting in a "surprising result" in terms of how much ADIs were willing to lend. "It was not uncommon to find the most generous ADI was prepared to lend in the order of 50 per cent more than the most conservative ADI," Byres reveals.

The APRA test uncovered a number of areas in which Byres suggests the regulator found some lenders' assessments to be insufficiently conservative. One "major concern" is that a number of ADIs made credit assessments based on a lower level of borrower living expenses than were declared by the borrowers themselves.

*"We certainly want to see competition between lenders and fully accept that different ADIs can have different risk appetites. And we are not seeking to interfere in ADIs' ability to compete on price, service standards or other aspects of the customer experience."*

WAYNE BYRES AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY

and has remained there since. Meanwhile, lower interest rates are giving housing near-term affordability. The concern felt by APRA and others is that lax lending standards could allow borrowers to take out loans they can only afford for as long as rates remain at emergency lows, while a further jump in unemployment could spark a dramatic spike in arrears.

However, lenders are confident that Australia is well positioned to cope with potential exacerbation of either of these two factors. Their view is that lending standards – with the help of APRA's review – are strong enough to prevent widespread bad credit emerging.

Taking a further step into the securitisation market, sources tell *ASJ* that factors like the prevalence of full-recourse loans and lenders' mortgage insurance (LMI) in the Australian

mortgage market mean local RMBS product has further built-in safeguards against economic travails (see box on p16).

### RESILIENCE CLEAR

Australia's economic challenges also suggest that the high lending standards to which mortgage-originators point are continuing to hold up – specifically the fact that the rise in unemployment has yet to result in a spike in mortgage arrears.

Speaking at a roundtable discussion hosted in March by *KangaNews* and RBC Capital Markets, Simon Maidment, Sydney-based deputy group treasurer at Commonwealth Bank of Australia, said: "The uptick in unemployment has been modest but there has not been even a commensurate increase in mortgage arrears, which remain incredibly low... Whether

Byres reveals: “Best practice – and intuition – would be to apply minimum living-expense assumptions that increase with borrower incomes; this was a practice adopted by only a minority of ADIs in our survey.”

APRA believes some lenders are also too lax in terms of how they assess other income sources, such as bonuses, overtime and investment earnings. “Common sense would suggest it is prudent to apply a discount or haircut to these types of income, reflecting the fact they are often a less reliable means of meeting regular loan repayments,” Byres argues. “Unfortunately, common sense was sometimes absent.”

Elsewhere, APRA found some ADIs applying smaller haircuts than the industry-standard 20 per cent – or even no haircut at all – on borrowers’ declared rental income, and some applying no interest-rate buffer to investment borrowers’ existing debts.

On this latter issue, Byres says: “I confess to struggling to see the logic of such an approach – after all, any rise in interest rates will at some point in time affect the borrower’s other debts just as they will for the new loan being sought.”

Finally, the APRA test uncovered some ADIs using overly generous projections of borrowers’ servicing of loans with interest-only periods. Even with a five-year interest-only period at the start of a 30-year mortgage,

Byres reveals, the majority of lenders assumed principal and interest repayment over the entire 30 years – and “hence were able to inflate the hypothetical borrower’s apparent surplus income by, in our particular example, around 5 per cent”.

#### CONCERNS MANAGED

Despite APRA’s findings so far in the review, Byres wasted no time in confirming the outcomes are not sufficiently concerning to bring new rules into practice. APRA’s next course of action is likely to remain at the micro, issuer-specific level.

Byres confirms that “Australian ADIs are thankfully well away from the types of subprime lending that have caused so many problems elsewhere, for example lending with a loan-to-value ratio in excess of 100 per cent, at teaser rates [or] to borrowers with no real capacity to repay”.

He highlights system-level regulatory options potentially available to APRA, including: “Additional supervisory monitoring and oversight, supervisory actions involving pillar-two capital requirements for individual ADIs, and higher regulatory capital requirements at a system-wide level. Beyond this, there are more direct controls that are increasingly being used in other jurisdictions, such as limits on particular types of lending – what are commonly referred to as macroprudential controls.”

However, he also points out that, to date, the Australian regulator has “opted to stick with traditional microprudential tools targeted at individual ADIs and their specific practices”. And he suggests that, at this point, the same strategy will be deployed to correct issues identified by the lending standards review.

“Our overall conclusion from this hypothetical borrower exercise was that there were clearly examples of practice that were less than prudent,” Byres concludes. “As a result, we have shown ADIs that participated in the exercise how they compare to their peers and where their serviceability assessments could be strengthened: in all of the examples... we expect to see changes to practices across a range of ADIs.”

APRA’s goal is not to standardise mortgage-lending standards. Byres says the regulator expects ADIs to adhere to “some minimum expectations” around things like interest-rate buffers and floors, and to “adopt prudent estimates of borrowers’ likely income and expenses”.

But, he adds: “We certainly want to see competition between lenders and fully accept that different ADIs can have different risk appetites. And we are not seeking to interfere in ADIs’ ability to compete on price, service standards or other aspects of the customer experience.”

it’s the banks or the regulators, all stakeholders have been keen to ensure lending standards don’t change at the wrong point in the cycle, which could leave a poor legacy. The fact that unemployment has been able to creep up a little without causing major stress shows we have robust lending standards.”

David Carroll, Fitch’s Sydney-based director, structured finance, agrees that Australia’s historically low level of arrears is indicative of quality lending standards. “In 2008-10, we saw higher arrears, off a very low base, as a result of lower economic conditions. However, arrears have since fallen to relatively low levels. Lending standards tightened after 2008 and levels of arrears have remained very low since,” he says.

The nature of the increase in unemployment has likely helped. Chaplin points out that because the unemployment

rate has picked up slowly over time, mortgage lenders, regulators and the government have all been able to adjust.

The same is true for mortgage holders themselves. “Those with financial difficulties can make adjustments through this period, and those who don’t have financial difficulties will, in times of caution, be prepaying heavily on loans to create a financial buffer,” Chaplin comments.

S&P does not view a slow adjustment in unemployment as anything like as concerning as a sudden shock. “Our forecasts do not predict such a shock,” Chaplin adds. “We expect unemployment to go up and we think the rebalancing of Australia’s economy could be slower than the market would like it to be, but unemployment is not likely to go up rapidly and cause a major collapse.”

## Re-evaluating LMI

AUSTRALIAN RESIDENTIAL MORTGAGE-BACKED SECURITIES (RMBS) HAVE HISTORICALLY BENEFITED FROM THE ADDITIONAL CREDIT SUPPORT OF LENDERS' MORTGAGE INSURANCE (LMI). PROVIDERS EXPLAIN WHY LMI CONTINUES TO PLAY AN IMPORTANT ROLE IN SUPPORTING THE MARKET'S ROBUSTNESS – DESPITE A RE-EXAMINATION OF THE ROLE OF MORTGAGE INSURANCE.

Jenny Boddington, executive general manager, financial institutions at QBE Australia and chief executive of QBE LMI in Sydney, says LMI providers act as a second set of eyes on the market. She comments: "One reason the Australian RMBS market did not experience similar problems to the US was that the prime RMBS market was indirectly regulated by the Australian Prudential Regulation Authority (APRA), through APRA-regulated LMI companies."

A similar message about the role of LMI in the Australian industry comes from Genworth. Its Sydney-based chief financial officer, Georgette Nicholas, explains: "We have a strong impact on providing insight on what is happening in the market."

Current economic and market conditions only enhance this role. "APRA is certainly helping with this, given it is an active regulator overlooking the lenders markets and creating a focus on investment properties by limiting growth to 10 per cent," Nicholas continues. "Given cash rates are dropping, this is an important part of managing risk with the variable nature of the market going forward."

### LMI CHALLENGES

LMI is clearly a market shaper in Australia – and is also facing challenges.

Most recently, a change in assessment criteria used for LMI by Standard & Poor's Ratings Services (S&P) put the whole industry under the microscope.

The new criteria came into effect on February 2 this year, following a request-for-comment (RFC) period which appeared to result in a shift in Australian issuers' ratings preferences on RMBS deals. Of the two prime RMBS deals which directly followed the RFC announcement, by AMP Bank and Beyond Bank, neither opted for an S&P rating.

The major changes between S&P's RFC proposals and its finalised criteria principally fall under "cancellable policy" and "rating differentiation for assumed claims-adjustment rates".

The first covers S&P criteria for assessing whether credit support is sufficient to cover potential losses after applying a 50 per cent haircut to the mortgage insurance coverage amount for cancellable policies based on two possible outcomes. The second is intended to simplify application and differentiates among claims adjustments by rating categories.

A day after the revised methodology was published, S&P lowered the ratings on 61 tranches

of Australian and New Zealand RMBS, and affirmed those on an additional 82 tranches. At the same time, the rating agency lowered its rating on QBE LMI to A+ from AA- with a stable outlook. At the same time, Genworth Financial Mortgage Insurance (GFMI) was affirmed at A+ with a developing outlook.

Meanwhile, as at mid-May 2015 QBE LMI is rated A2 and AA- by Moody's Investors Service and Fitch Ratings (Fitch), while GFMI holds A3 and A+ ratings from the same rating agencies.

However, while market feedback was clouded with uncertainty at the time, since implementation of the new methodology the market has returned to its historical norm – where S&P and at least one other rating agency typically provide ratings to Australian prime RMBS deals.

Boddington says the S&P changes were not unexpected. "The market was aware that S&P had been conducting the methodology review for several months. QBE has not received any negative feedback from clients following the changes," she tells ASJ.

But Nicholas points out that alongside the market uncertainty surrounding S&P's review, Genworth's clients are also faced with the challenge of assessing how mortgage lending standards may develop and what impact this might have from a cost perspective. "This depends on the types of tranches and types of notes in the transaction and whether it makes economic sense to include LMI."

### MOVING FORWARD

The industry has dealt with issues before. The first major one emerged in the wake of the financial crisis: concerns about the ability of insurers with



*"Investors are increasingly looking through LMI given recent changes by the rating agencies and the downgrading of the insurers themselves. We may see some different types of structures issued given the changes in rating agency methodology and in investor appetite for risk."*

JOHN CAELLI ME

substantial exposure to a single risk factor – in this case, Australian housing – have led to heightened rating-agency scrutiny.

On May 12 this year, Moody's published a report stating that Australian mortgage insurers are well positioned. According to the report, the Australian LMI sector remains financially sound with healthy capital levels, good underlying profitability and solid underwriting practices.

In fact, the challenges the sector faces are mainly on a business level. The rating agency states in the May report: "Recent moves by some Australian banks to diversify their mortgage insurance to more diverse global reinsurers, and the increase in the use of self-insured, low-deposit mortgage products, could over time threaten the lenders' mortgage insurers' future prospects."

Australian LMI providers insist that RMBS issuers continue to be engaged with LMI. The decision to use LMI as a tool for credit enhancement when structuring an RMBS deal will vary for each transaction.

In funding-only transactions, Boddington explains, the issuer tends to retain most of the subordinated notes and therefore does not generally need to rely on LMI as a credit-enhancement tool. There is stronger reliance on LMI for funding and capital relief transactions, in which mezzanine and subordinated notes are typically sold to third-party investors rather than retained by the issuer.

"We anticipate that potential growth opportunities will come from major banks if they start to issue RMBS for both funding and capital purposes," Boddington says.

### SMOOTHING EFFECT

The providers remain confident in the value of their product in a downturn. "While Australian mortgages are performing well at the moment, we know that when the market experiences stress – as it undoubtedly will do at some point in the future – we will see a divergence in loan performance. LMI will smooth this for investors," Boddington argues.

Nicholas also points to the importance of investor education in order to actively promote the value of LMI. This is particularly important given the securitisation market seems to be balanced between issuers deciding whether LMI makes sense from an economic standpoint, and investors looking at the market from a yield perspective.

In fact, Nicholas suggests, LMI is an important part of the value chain of Australian mortgage origination. "For Genworth, the challenge is educating investors that we do more than just pay a claim. We are part of quality assurance up front – we work with lenders and do a lot around the underwriting side, to audit and assess underwriting quality across the market," she tells ASJ.

LMI providers such as Genworth point out that they also offer support by managing aspects of the arrears segment of the mortgage market, Nicholas explains. "We audit the underwriting quality of a transaction's book before it goes to market. If it goes delinquent, we have a strong arrears-management and loss-mitigation process to go through. There are services, such as this, which we provide which perhaps are not fully appreciated at a time when the market is good, but are important in times of stress."

### ISSUER PERSPECTIVE

Issuers themselves appear to continue to value the part LMI plays in Australia's mortgage market, but note that going forward there may be a shift in its usage in RMBS structures.

Peter Casey, deputy treasurer at ING Bank Australia, points out that only one of the bank's eight IDOL Trust RMBS transactions since 2010 has not had all the loans insured. He explains that investors put particular value on insurance of high loan-to-value ratio (LVR) loans. For lower LVR loans they are open to receiving greater credit enhancement through the structure rather than through LMI.

"This trend – prompting issuers to think about whether they get value for insurance – may gather pace, although we haven't seen this happen yet," Casey comments.

But he agrees that LMI providers give investors the added benefit of a third party which has the same interests as them. "The insurer wants those loans underwritten and serviced well, and so do investors. This gives further confidence in the market."

As another regional bank lender, ME's general manager, markets, John Caelli, agrees that LMI has played an important role in the mortgage market historically. But he adds that going forward structures will need to "stand on their own two feet" irrespective of LMI. "Investors are increasingly looking through LMI given recent changes by the rating agencies and the downgrading of the insurers themselves," Caelli comments. "We may see some different types of structures issued, given the changes in rating-agency methodology and in investor appetite for risk."

*"We audit the underwriting quality of a transaction's book before it goes to market. If it goes delinquent, we have a strong arrears-management and loss-mitigation process to go through. There are services, such as this, which we provide which perhaps are not fully appreciated at a time when the market is good, but are important in times of stress."*

GEORGETTE NICHOLAS GENWORTH



## Reporting benefits

THE RESERVE BANK OF AUSTRALIA (RBA) IS ASKING BANKS TO PROVIDE MORE LOAN-LEVEL DATA ON RESIDENTIAL MORTGAGE-BACKED SECURITIES (RMBS) TRANSACTIONS AS PART OF ITS REPO-ELIGIBILITY CRITERIA. BANK AND NONBANK ISSUERS SEE POSITIVE CONSEQUENCES – DESPITE THE OPERATIONAL CHALLENGES.

Issuers of eligible RMBS will be required to provide loan-level, security-level and cash-flow waterfall data for repo-eligible transactions on a monthly basis. These data requirements will become mandatory as of June 30 2015. RMBS issuers say the RBA requirements should also have positive consequences for the market – once the operational issues have been worked through.

Guy Volpicella, head of structured funding and capital, group treasury

at Westpac Banking Corporation, explains that the process will create a consistent framework from which comparative analysis will become easier. “The key benefit to more regular and consistent reporting is that there will be easier comparability of assessments. This consistency is key to developing more useful research,” he tells *ASJ*.

Other market participants are equally positive about the reporting requirements but add that, as

of mid-May 2015, the majority of mortgage originators’ energy is going into preparing for data collection itself. Only once the data has been collated and analysed do issuers agree there will be more clarity on the subject of how the process will shape the securitisation market into the future.

“It will be great to have standardised reporting – we are confident this will be good for the market,” James Austin, chief financial officer at Firstmac, suggests. “I don’t think RBA reporting will affect deal structures or capital pools but instead it will act to illuminate the quality of the product already there. Local investors already have access to this information directly from the issuers, and it may be that offshore investors will in future get the opportunity to access information more readily.”



*“I don’t think RBA reporting will affect deal structures or capital pools but instead it will act to illuminate the quality of the product already there.”*

**JAMES AUSTIN** FIRSTMAC

In fact, according to a report published on May 18 by S&P, housing loans in arrears decreased further for prime RMBS in the March quarter – though they ticked upwards for nonconforming RMBS. Loans in arrears greater than 30 days underlying Australian prime RMBS decreased by 10 basis points in March, to 1.05 per cent. Nonconforming RMBS arrears increased by 59 basis points, to 6.11 per cent, in March.

Another reason why unemployment has not sparked arrears so far may be the fact that, while the focus of regulators is on the extremes of the lending market, the overall quality of the Australian mortgage book is extremely high. The housing market in Australia is in aggregate still lightly geared, with high-LVR lending forming a relative small portion of origination.

Guy Volpicella, head of structured funding and capital, group treasury at Westpac Banking Corporation (Westpac) in Sydney, reveals: “Every new mortgage which comes on board has an equity contribution on average of about a 30 per cent down-payment, so our average LVR on day one is closer to 70 per cent. This creates an immediate buffer.”

He adds that the propensity for mortgage owners in Australia to pay their loans ahead of schedule – given the tax system gives an incentive to do so – means the average dynamic LVR of Westpac’s book is only around 43 per cent.

Borrower conservatism in the wake of the financial crisis means most are multiple payments ahead of repayment schedule, and are thus insulated against temporary periods of financial uncertainty.

### INVESTORS FOCUSED

It is these factors supporting Australia’s robust mortgage lending standards which enable mortgage lenders to successfully market the quality of underlying mortgage loans to investors, both on- and offshore.

John Caelli, general manager, markets at ME in Melbourne, says the bank focuses on the very low arrears in its RMBS pools as well as pool seasoning and low average LVR when discussing the quality of underlying loans to investors.

Similarly, Peter Casey, deputy treasurer at ING Bank Australia (ING) in Sydney, comments that he often receives questions about the quality of loans and underwriting from investors. He adds that on some occasions it has taken a while for investors, especially those from offshore, to get comfortable with Australian loans.

But Casey also says: “Australia’s economics helps, as does its solid history of loan performance. ING has been issuing for five years so has started to make a name for itself – we can show a

track record of good-quality performance. We have also done a lot of work around explaining the serviceability modelling we use, in which our focus is ensuring the borrower can meet repayments.”

Similarly, nonbank issuers have also found that Australia’s performance history and demonstrable credit metrics have greatly supported the ability to market to investors. “It is not difficult to market our Australian mortgage portfolios offshore, because performance metrics are outstanding on a global basis,” Mary Ploughman, head of capital markets at Resimac in Sydney, tells *ASJ*. She adds that being able to explain how the Australian economy moved through the financial crisis has benefited Resimac. In this context, the fact that Australia did not experience a recession but local sentiment was still and significantly shaken by the global events has produced positive outcomes.

“The current environment, where Australia has very low interest rates, has translated into borrowers using the time to improve their personal balance sheets, pay down mortgages and get ahead of schedule,” Ploughman explains. “It is easy to highlight the attributes of our RMBS pools given the amount of things which have improved over time – specifically lower LVRs.”

## BUBBLE TALK

Despite the improvements in Australia’s mortgage market, rising house prices, particularly in Sydney and Melbourne, have garnered a lot of buy-side attention. One of the most common questions asked by investors, particularly offshore, is about whether a bubble is inflating in Australia.

Caelli says that in response to these queries he tends to point to the good performance of property prices through the cycle, and also to the level of owner-occupier loans. “I’m not convinced what we have in Australia could be called a bubble – there is enough fundamental support to suggest limited risk of a sudden and significant correction in prices,” he comments.

Meanwhile, Casey argues that well-seasoned loan portfolios also add a buffer. “The price of a property which has a five-year-old loan could have significantly increased in value during that time. So even if there is a fall in property

*“It can take a while for investors to get comfortable with Australian loans. Australia’s economics helps, as does its solid history of loan performance. We have also done a lot of work around explaining the serviceability modelling we use.”*

**PETER CASEY** ING BANK AUSTRALIA



value, there is a long way to go before it gets back to its original value,” he explains. “This is also a factor which rating agencies consider – how old is the loan and what could happen to the price of property in the meantime?”

For Volpicella, the key elements to consider are the current supply-demand imbalance, the fact that only about 40 per cent of homeowners have a mortgage, the full-recourse nature of the product and the low level of overall gearing, as a result of the initial equity contribution and early repayments.

“These factors reduce the propensity for a large number of property owners to be forced sellers. Unless they are forced, people do not sell their house just because the value of their property goes down – a home loan is not like a margin loan. As long as you continue making your mortgage payments, or remain ahead of your scheduled payments, the bank isn’t going to come knocking on your door,” he comments.

James Austin, chief financial officer at Firstmac in Brisbane, acknowledges a heightened level of scrutiny from investors and regulators – but says Australian issuers are applying the same rigour as they always have. “Investors are requesting a lot more analysis on the quality of the borrower, income levels and their serviceability,” he reveals. “In years gone by investors didn’t seek the same detailed level of data as they do today, albeit it has always been available directly from the issuer – just not in a public forum.”

Increased clarity around the topic should help manage these concerns for investors. In fact, Ploughman says the focus on a possible housing bubble appeared to have eased when Resimac met offshore investors in February. “Resimac will be on the road again quite soon. We will need to be very clear about servicing – our serviceability test ensures people can service way above interest rate levels,” she adds. “We still have a good story to tell, but there is uncertainty out there. There aren’t predictions of significant growth, but there isn’t expectation the market will fall off a cliff either.” ■

*“In the US and Europe there has been some tightening of lending criteria. As a result, in the current Australian environment of high house prices, interest-rate cuts and housing-market competition, I’m not sure claims that Australian mortgage-lending is of a higher quality than elsewhere are still as true as they were a few years ago.”*

**JENNIFER WU** MOODY’S INVESTORS SERVICE



# MACROPRUDENTIAL MEASURES IN AN AUSTRALIAN CONTEXT

*As concern lingers over household indebtedness and rising property prices in Australia, the most recent interest-rate cut by the Reserve Bank of Australia (RBA) has reignited a debate over macroprudential measures and their application in Australia. Erin Kitson, structured finance analyst at Standard & Poor's Ratings Services (S&P) in Melbourne, looks at how Australia shapes up globally.*

**R**egulatory intervention in the form of macroprudential measures has been implemented in several countries as a way of stemming property prices and slowing credit growth. Countries such as New Zealand and the UK, for example, have implemented macroprudential measures to help slow housing-related credit growth and house-price inflation in a bid to reduce the risk of a material decline in property prices. However, it is difficult to isolate the effectiveness of the measures from other economic influences at play.

In S&P's opinion, macroprudential measures in Australia will be focused on ensuring the nation's banks and households are well positioned to absorb any potential fallout from a rapid fall in property prices, consistent with the RBA's financial-stability objectives. To this extent, we believe any resultant rebound in residential property-price growth might be viewed as a secondary outcome.

We believe the strong growth in Australian residential property prices can be partly attributed to factors other than lending practices and credit growth, including strong immigration inflows and supply constraints, and is to an extent outside the direct reach of prudential oversight.

Australia has adopted a more principles-based approach to macroprudential measures than jurisdictions such as New Zealand and the UK. From our observations, Australian lenders appear to have heeded regulators' warnings, and have so far avoided the necessity of a more prescriptive approach on the part of the local regulators.

Consumer-credit legislation, which has been in place since early 2010, largely leaves mortgage underwriting decisions in Australia to the lender. The legislation requires lenders to take reasonable steps to confirm and demonstrate that a borrower will be able to repay a loan.

This has contributed to an overall decline in low-documentation lending: low-documentation loans as a share of new lending fell to 0.70 per cent in March 2015 from 11.50 per cent in March 2008, according to Australian Prudential Regulation Authority (APRA) statistics.

Australian regulators have in recent months increased their focus on higher-risk lending, given the low interest-rate environment and strong growth in investor and interest-only lending. In late 2014, APRA released a practice guide on sound home mortgage practices and established some benchmarks on certain aspects of banks' housing lending standards.

In December 2014, the Australian Securities and Investments Commission (ASIC) announced a review of interest-only lending. Both APRA and the RBA are monitoring the effects of these measures, but it is too early to judge their effectiveness, according to recent comments by the RBA's governor, Glenn Stevens.

## MACROPRUDENTIAL AND PRUDENT LENDING

Macroprudential measures adopted by other countries have taken on a wide variety of forms – with mixed effects – and are country specific. While some measures have been effective at dampening house-price inflation or credit growth in the short term, the timing of implementation of such measures has been challenging.

## LVR LIMITS

We believe that capping loan-to-value ratios (LVRs) could dampen credit extension to marginal borrowers who have limited deposits, while not necessarily dampening house price growth. Lending practices and credit growth affect property prices, and factors such as rising demand as a result of strong immigration, supply constraints, and favorable tax treatment for investment properties serve to drive up the prices. Furthermore, most lenders already use LVR ratio limits to manage their loss exposure.

Total exposure to loans with an LVR above 80 per cent is just less than 20 per cent across the Australian residential mortgage-backed securities (RMBS) sector, as rated by S&P. We believe a rise in LVR exponentially increases borrower default risk and raises loss exposure to a borrower default. Australian lenders typically take out lenders' mortgage insurance for loans with LVR of 80 per cent or greater, to redistribute risk. Furthermore, RMBS with greater exposure to high LVR loans typically have higher credit enhancement for senior notes, to minimise losses.

In New Zealand, LVR limits were introduced due to ongoing reserve bank concerns over house-price inflation. These took the form of a cap of 10 per cent of new residential

loans to borrowers with LVRs of more than 80 per cent.

According to Reserve Bank of New Zealand statistics, lending at LTV ratios above 80 per cent as a share of total new mortgage commitments has declined since the measure was implemented. However, the effect of LVR restrictions seems to have been limited at best, given the strong growth in Auckland property prices.

## DEBT-SERVICEABILITY LIMITS

APRA's latest practice guide expects a combination of buffers and adjustments in banks' debt-serviceability assessment models. We

believe improving affordability assessments can help lessen the effects of weakened wage growth and rising interest rates on borrowers. When a borrower's ability to service a loan is weak to start with, any shock caused by increased interest payments, living expenses, or a partial reduction in income could result in financial difficulty, and potentially to default.

However, the effectiveness of debt-serviceability limits on property prices and credit growth might be mixed, because many lenders already incorporate interest-rate buffers in their debt-serviceability assessments in order to minimise the aforementioned shocks. In the context of investment-property lending, debt-serviceability risk is partly reduced by the cohort of borrowers to which these loans are extended – because the typical borrower for an investment loan is in a higher income and net-worth bracket.

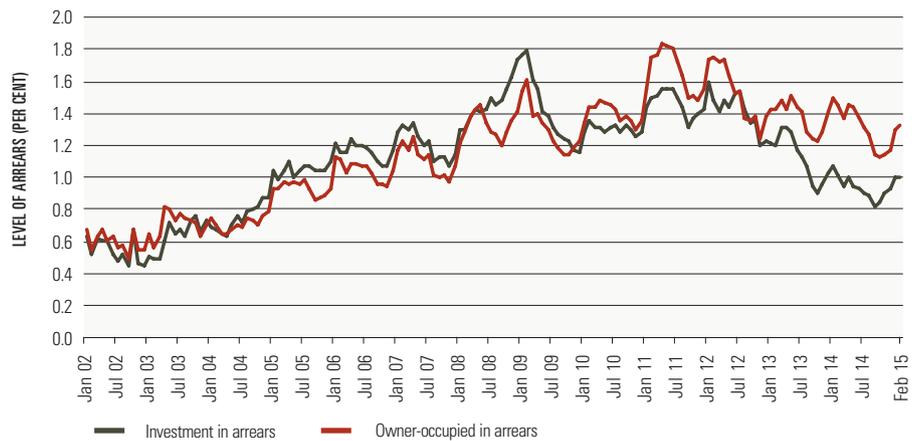
Debt-serviceability limits have been widely used in countries such as Singapore and South Korea. More recently, the Bank of England introduced loan-to-income limits and mortgage-affordability tests. We believe stricter underwriting criteria and standards in the UK have improved the credit quality of loans originated since their implementation. However, it is difficult to isolate the effect of these measures on house prices and mortgage performance from other macroeconomic influences, such as a decline in the UK's unemployment rate.

## SECTORAL CAPITAL REQUIREMENTS

Sectoral capital requirements that differentiate between the capital treatment for investment loans and owner-occupier loans could slow the growth of investment-property lending due to increased funding costs from higher capital charges.

This could in turn affect the composition of mortgage pools underlying Australian RMBS. Around 26 per cent of loans underlying Australian RMBS transactions are currently for investment purposes. This figure could fall if investment loans attracted a higher capital charge, and it was applied uniformly across the lending sector. One of the key differences between

## AUSTRALIAN INVESTMENT VERSUS OWNER-OCCUPIED ARREARS



SOURCE: STANDARD & POOR'S RATINGS SERVICES MAY 2015

investor loans and owner-occupier loans is the rate at which equity is built up in the loan. Owner-occupiers in Australia typically try to repay their home loans as quickly as possible, because there is no tax incentive to delaying payment and repaying a home loan is an effective way of saving.

Conversely, investors who are less incentivised to repay loans quickly gain equity more slowly. This is also the case for interest-only loans. While we have not observed any significant performance differentiation between loans extended to investors and owner-occupiers in the current benign economic environment, performance may diverge during a more severe economic downturn (see chart on this page). Another concern is that investment property loans driven by speculative behaviour could contribute to price volatility.

More recently, Sweden and Norway have introduced floors on risk weights for home loans to further strengthen banks' resilience against housing-market shocks. In New Zealand and the UK, proposals are under consideration regarding differential capital treatment between owner-occupier and investment loans.

## AUSTRALIAN LENDERS REQUIRE SELF-DISCIPLINE

The more subdued economic climate in Australia underlines the importance of responsible lending practices to help minimise the incidence of borrower default and the risk of large property-market corrections. While the effectiveness of macroprudential measures in averting a property-price correction remains a subject of much debate, a prudent, self-disciplined approach by Australian lenders might mean a more prescriptive regulatory approach is unnecessary.

*Under S&P's policies, only a rating committee can determine a credit rating action, including a credit rating change, affirmation or withdrawal, rating outlook change, or credit watch action. This commentary and its subject matter have not been the subject of rating committee action and should not be interpreted as a change to, or affirmation of, a credit rating or rating outlook. ■*

# On the acquisition trail

*Australia's secondary loans market has picked up pace in recent years, as capital pressures and business realignment have combined with ambitious purchasers to see a raft of loan portfolios changing hands. Residential mortgage books have been the most commonly transacted assets, but there has also been a steady – and growing – market for consumer-finance receivables and other asset classes, including deals with an international flavour.*

*Acquirers include both bank and nonbank entities. In the latter case, securitisation technology tends to be used in the acquisition-finance packages put together to fund transactions. For both types of buyer, access to the securitisation market in the medium and longer term tends to be a critical part of the business case for acquisition.*

*In May 2015, ASJ talked to three Australian firms responsible for some of the most successful recent securitisation-relevant acquisitions, a leading legal adviser, as well as the sponsor of this project, **National Australia Bank** (NAB) – a key senior lender to many transactions. Their comments give an unrivalled insight into the process, the challenges and the achievements.*

## PARTICIPANTS

- ◆ **Berkeley Cox** Partner KING & WOOD MALLESONS
- ◆ **Mike Culhane** Co-Group Chief Executive Officer PEPPER GROUP
- ◆ **Jacqueline Fox** Head of Securitisation Originations NATIONAL AUSTRALIA BANK
- ◆ **Tim Ledingham** Treasurer BANK OF QUEENSLAND
- ◆ **Anne-Marie Neagle** Partner KING & WOOD MALLESONS
- ◆ **Mary Ploughman** Head of Capital Markets RESIMAC
- ◆ **Patrick Tuttle** Co-Group Chief Executive Officer PEPPER GROUP

## MODERATOR

- ◆ **Laurence Davison** Managing Editor KANGANEWS

## ACQUISITION HISTORY

**Davison** *Can the participants give a brief overview of their experiences with acquisition of securitisation-related portfolios and entities, and what these acquisitions have meant in business-development terms?*

◆ **PLOUGHMAN** We have successfully completed three acquisitions, including that of the RHG Mortgages (RHG) portfolio. RHG fits very well with our business, because the product suite of what comprised the old RAMS business, which became RHG, was very closely aligned with that of Resimac.

The key thing that makes these transactions successful is the combination of a willing buyer and a willing seller. We have wasted time on deals that have ultimately been withdrawn or where there has been what we perceived to be another agenda at play. But when there is an open market process we are very happy to engage with it.

I am happy to say I think there will continue to be opportunities. This is particularly so given we are in an environment where there have been changing capital requirements – there may be opportunities caused by banks selling portfolios which are high users of capital.

◆ **LEDINGHAM** Bank of Queensland (BOQ) has made two acquisitions of assets with securitisation capabilities. The first was the auto- and equipment-finance book of UFJ, in October 2003. This had an existing securitisation programme, called Symphony, which had made a number of issues in the public market prior to the acquisition. Our REDS asset-backed securities programme was established in order to take out some of the acquisition finance used for the UFJ purchase.

Then last year we acquired the Investec Bank Australia (Investec) business. This is largely a professional finance business for doctors, dentists, accountants and some financial planners, with loans made against assets such as business premises and medical equipment. It also has relationship-based distribution, through professional associations.

It's fair to say that the assets secured under Investec's Impala programme have a different profile from REDS.

◆ **CULHANE** Everything changed for Pepper Group (Pepper) when ownership changed, in June 2010. From this point on we have been quite acquisitive. The first big portfolio acquisition was in early 2011, which was the GE Capital Australian residential mortgage portfolio – of A\$5 billion (US\$4.0 billion).

The only reason we were even able to contemplate this purchase was the fact that we had been focusing on third-party servicing alongside mortgage origination since 2008. We had experience servicing third-party portfolios on behalf of banks, which had taken them back on balance sheet from nonbank originators when they hadn't, perhaps, been expecting to – as a consequence of the financial crisis.

The scale of the GE Capital portfolio was overwhelming to start with. But, on the other hand, we had tremendous



operational and financial support from our banks when we told them it was something we were interested in exploring. Our view at was that the GE Capital portfolio was not performing as it should, largely because it was not being serviced as it should.

What we had to do was pull together all the financing – from the senior lenders, mezzanine investors from both on- and offshore and our own equity contribution at the bottom. We took the proposition to GE Capital with the offer to take, substantively, all the people working on the portfolio and the technology. It was therefore a very clean deal, which we believe helped us win the bidding process.

♦ **TUTTLE** Securitisation finance was crucial to the deal. We had to establish seven bilateral warehouse facilities to acquire A\$5 billion of assets: two in New Zealand and five in Australia, provided by three senior funders. We were leveraging the same securitisation structures we had in our traditional warehouses and in our public transactions. As a nonbank lender, this is really the only way we can efficiently fund an acquisition of this size.

Following on from the GE Capital deal in Australia, our next acquisition was in Ireland. Again, we used securitisation technology to buy GE Money's highly distressed residential-mortgage portfolio valued, at today's exchange rate, at A\$913 million.

We made a small co-investment in the underlying loan book and were appointed as the servicer and trust manager of an Irish special-purpose vehicle. This was the genesis of our whole Irish loan-servicing business.

Including the loan portfolios in which we have an economic interest and those which we manage on a purely fee-for-service basis, our Irish business now has in excess of €13 billion (US\$14.9 billion) in assets under management.

♦ **COX** We have been fortunate to represent, for a long time, a range of the nonbank originators in the Australian market which have been active secondary loan-market participants.

Going back to 2006 – when Firstmac bought a portfolio of mortgage loans from HSBC – we have also acted on many of these nonbanks' acquisitions. Until these types of transactions, the secondary loan market in Australia was virtually non-existent – certainly compared with the much more active equivalent in the US.

A set of practices and documents has been developed to facilitate nonbank originators setting funding structures to

issue debt on the day of a transaction closing, usually on a private or warehouse basis, with proceeds of this debt used to acquire the assets.

The nonbanks have been active players in the secondary loan market in Australia, but regulated entities have also been participants. When these entities take part they tend to fund acquisitions off their own balance sheets on day one, rather than through securitised funding structures.

Major transactions include Pepper's A\$5 billion acquisition from GE Capital in 2011, which involved the prime and nonconforming mortgage asset classes.

♦ **NEAGLE** In recent years we have seen examples of securitisation technology being used both as part of asset-level acquisitions and as part of acquisitions of shares in a target owning the underlying assets. In the latter case, there is a simultaneous securitisation of some of the assets owned by the acquired entity.

Most of the acquisitions we have seen in the Australian market have been of mortgage assets, but there has also been in activity in other asset classes. For example, we have been fortunate to have recently assisted a consortium of China Travel Financial Holdings, Pepper and York Capital Management Global Investors to acquire and finance a substantial consumer credit business in Hong Kong and China.

**Davison** *As Berkeley Cox says, banks – like BOQ – can conduct acquisition finance on a bilateral basis, without having to include a group of senior and mezzanine lenders. How did this bilateral process work in the Investec purchase?*

♦ **LEDINGHAM** It was a fully funded book, so we were acquiring a deposit portfolio, a liquid-assets book and some other wholesale debt as well as the Impala programme. The purchase therefore did not require the same kind of financing: we were largely paying for the net assets and any premium. To put this in perspective, the value of the acquisition was around A\$2.5 billion, or A\$3.0-3.5 billion with the liquid assets included. This is not huge in the context of BOQ's A\$40-50 billion balance sheet.

BOQ conducted a rights issue to provide the equity funding for the acquisition, as the bank deemed common equity to be the most appropriate and effective means of achieving capitalisation at that point in time.

**“WE AREN'T LOOKING AT OUR INVOLVEMENT AS A BUY-AND-HOLD PROCESS. WE SEE IT AS AN INTERMEDIATION: WE ARE HELPING OUR CLIENTS TO GROW THEIR BUSINESSES OVER TIME, AND TO REALISE THE FULL VALUE OF THEIR PURCHASES.”**

**JACQUI FOX** NATIONAL AUSTRALIA BANK



## Changing market

THE FINANCIAL CRISIS MIGHT HAVE BEEN EXPECTED TO HAVE THROWN OFF PLENTY OF DISTRESSED LENDING-BOOK SALES. BUT AUSTRALIAN BUYERS SAY NON-CORE ASSETS ARE MORE FREQUENTLY SEEN ON THE SELLING BLOCK THAN GENUINELY DISTRESSED ONES.

**Davison** *In terms of future acquisition prospects, is it reasonable to think that we might be moving from a period of distressed sales of nonperforming businesses – which of course might still represent good value – to one where portfolios being sold off are more likely to be non-core? In other words, banks selling portfolios which no longer hold as much value to them in the new capital environment.*

**PLOUGHMAN** There has not been a significant quantity of distressed sales of asset portfolios. There has been some of this kind of activity in New Zealand, and we have picked up some assets there.

It is already the case that the majority of sales taking place in Australia have been around capital or other strategic decisions to exit a business – sales of assets considered non-core, in other words. I think there will be more of this.

An example of this is ING Bank Australia's sale of its mortgage-manager-originated portfolio.

**FOX** I think this observation is right. There has been some larger-scale asset divestment which has tended to be associated with parent decisions: the sale of portfolios by Lloyd's Banking Group and GE are examples. But a lot of books have managed to continue returning value, even in run-off. There may have been more activity if things had got worse in Australia.

**Davison** *If future asset sales in Australia are likely to be of non-core portfolios, should we expect activity to be concentrated in areas outside prime residential mortgages, too – like consumer receivables and nonconforming mortgages?*

**PLOUGHMAN** Yes – anything which requires higher levels of capital usage on the part of regulated lenders. There will be higher capital requirements for mortgages, but they will remain relatively capital light.

**FOX** I agree. We have recently seen ANZ Banking Group's Australian Securities Exchange statement regarding the proposed sale of the Esanda Dealer Finance division, while GE has reinforced its intention to divest the remaining GE Capital business where possible. We might also see consolidation around much smaller lenders – those we don't typically see in public securitisation markets.

**TUTTLE** Sometimes one can end up with a 'stub' pool of assets which doesn't

**Davison** *It seems acquisition has been a major contributor to growth for nonbanks in particular. How do these firms think about the concept of growth by acquisition, and how do they identify opportunities?*

◆ **CULHANE** I think the important point to make is that our approach to acquisition is very targeted. It goes back to our business planning from five or more years ago – around how we wanted to grow overseas and to take advantage of distressed assets.

We identified four markets in which we wanted to be active: the UK, Ireland, Spain and Italy. So far we have established a presence in the UK, Ireland and Spain – and we continue to look at Italy.

The reason for this plan was that there was a huge amount of distress in those markets, but at the same time we knew which management teams and platforms we wanted to get hold of. We knew banks were going to have trouble managing their portfolios and would want help managing them, we knew there were performing assets out there and, ultimately, we knew that we wanted to lend.

It has been very much a sequenced approach. We start with servicing, manage portfolios and then start lending. We are lending in Spain and the UK already, and we will do so in

Ireland in the next year or two. We have struggled to find a platform to buy in Italy, otherwise we would be there as well.

◆ **TUTTLE** Other than our acquisition in South Korea – which is a mutual savings bank – we use securitisation funding to lend in all the markets in which we have made platform acquisitions, including the UK, Spain and Hong Kong.

We have established senior and mezzanine warehouse facilities in the UK, for instance, to facilitate our re-entry into the nonconforming residential lending market. These warehouse facilities will be termed out through residential mortgage-backed securities (RMBS) transactions over time. It is the same story in Spain, albeit for a different asset class: being point-of-sales finance and personal loans.

We have also used securitised funding for the first time – to our knowledge, at least – in the Hong Kong market, to acquire PrimeCredit's personal-loan portfolio. In time we would like to take this approach to China. PrimeCredit has a small subsidiary in Shenzhen, which is largely debt funded. The securitisation market is very nascent in China, though, so it may be a while before we can go to the public debt markets there.

◆ **PLOUGHMAN** Resimac recognises it is in a volume business. We lost volume through the financial crisis, but we maintained a very sophisticated system. What acquisition has done – particularly that of RHG, the most high-profile acquisition we



fit current public securitisation criteria. This is where the flexibility our senior banks offer us can again be quite helpful, by adapting the underlying credit enhancement required to maintain these loans on a warehouse basis, for example, until they run off.

It can require more flexibility on both sides. For instance, we might have to put up more cash collateral to provide more comfort to a bank around nonperforming loans in a portfolio.

This isn't a huge proportion of the volume we see. The key is having very consistent loan-servicing techniques, across all the different asset classes, to give investors confidence that they are getting the same standard of post-settlement loan servicing across the Pepper Group programme – whether assets are originated by us or acquired.

**CULHANE** We bought a small portfolio of auto- and equipment-leasing

receivables from Suncorp in 2012, which wasn't big enough to securitise and effectively ran off. The senior funder was happy to let this happen – though it was quite a short-duration portfolio. It never appeared in any securitisation deal.

We also bought a book of small-balance commercial real-estate loans from Citi's non-core book in 2013 and, although we haven't ruled out starting to originate into this, I suspect it will simply run off as well.

**Davison** *Do you think there is a chance that this type of consolidation could be quite*

*positive for the Australian securitisation market, in the sense that it brings some assets from outside the public-market arena into the fold of originators that will add them to securitisation pools?*

**PLOUGHMAN** This is exactly what I think will happen. I am excited about developments like the divestment of GE Capital's assets – this activity, for example, is bringing more to the securitisation world. It was the same when we bought RHG Mortgages. All this activity makes the securitisation market deeper, and I think it is a very positive story for our bond market.

*“It is already the case that the majority of sales taking place in Australia have been around capital or other strategic decisions to exit a business – sales of assets considered non-core, in other words. I think there will be more of this.”*

**MARY PLOUGHMAN** RESIMAC



have made – is bulk up our business and spread the cost of our system across bigger asset volume.

There have been a number of opportunities for us to bulk up our volume over the past few years, notwithstanding the fact that we have a very strong organic-growth platform. At the same time, if there is an opportunity to grow via acquisition – especially of businesses that fit very well with what Resimac already does – we will be interested.

## DUE DILIGENCE

**Davison** *What are the challenges of due diligence in securitisation acquisition?*

♦ **NEAGLE** Due diligence depends to some extent on the approach the vendor and the purchaser take to allocating the risks in the acquisition. Ultimately, risk allocation will result from a combination of the due diligence undertaken by the purchaser, the information provided by the vendor – including any vendor diligence offered – and the package of protections that can be negotiated. This can include representations, warranties, indemnities and other protections.

What this means is the extent of due diligence can vary, depending on the legal mechanisms used to allocate risk and the residual risk the parties are willing to bear.

♦ **COX** When the assets being purchased involve retail consumers it introduces additional regulatory considerations in due diligence for analysis on top of contractual considerations.

It's important to look at the terms of the underlying assets and undertake some sampling of actual loan contracts, to make sure they are enforceable both contractually and in terms of original compliance with applicable consumer laws. The other issue is to make sure there is no limitation on assignment without consent of underlying borrowers.

In the case of secured finance contracts – which in most cases they have been – sampling around the effective registration of security documents would also be prudent.

♦ **PLOUGHMAN** Resimac has very strict criteria when we go down the acquisition path. In order to invest in any acquisition it needs to meet investment-committee criteria, both in terms of the Resimac business and – especially if there is a requirement for an additional capital injection – from the broader group.

We run a strict process. In the case of RHG, because it was a competitive auction we unfortunately needed to go through this process multiple times as the bidding continued.

We have been able to hone the process as we have been through it a number of times, with RHG being the most high

## Mezzanine finance

HUNGRY NONBANK BUYERS AND WILLING BANK SENIOR LENDERS MAKE A HANDY COMBINATION IN THE SECURITISATION ACQUISITION CHAIN. THE MIDDLE PIECE OF THE FUNDING EQUATION CAN BE READILY AVAILABLE, TOO – ALTHOUGH THE POOL IS DEEPER THAN IT IS WIDE.

**Davison** *It seems that there is good support available from senior lenders to acquirers in the securitisation sector. How important a role does mezzanine finance play?*

**CULHANE** For us, the bulk of the senior funding for the GE Capital acquisition was provided by our bank lenders – they really backed us. From there the question was adding the mezzanine piece. We had worked with these lenders previously, and in different jurisdictions, but not on an Australian whole loan. It was a new situation for them.

**TUTTLE** Experience is also very important here, and we probably have more experience than anyone in Australia in negotiating quite complex inter-creditor rights between senior and mezzanine funders.

There can be tension between the banks in the senior lender group and the investors at mezzanine level. I believe we are able to see the perspective of both, thanks to our experience going back to the original GE Capital acquisition in Australia.

**PLOUGHMAN** Mezzanine is the most important piece – it’s absolutely key. These lenders have to do a lot of work to understand a programme and what we as an acquirer are seeking to achieve. The size of investment is less but the work is more.

What’s interesting is that mezzanine lenders are the ones who are most keen for us to do bigger acquisitions. Their piece of the pie is relatively small proportionally, so their view is if they are going to do the credit work required to get comfortable, having done so they want to be involved for as big a transaction as possible. They also like to see other lenders in tranches.

Resimac sees itself as having customers at both ends of its business. There are the borrowers – the mortgage holders – but equally there are our investors. This doesn’t just mean the senior lenders and warehouse providers. Everyone in the structure is important.

Structured deals work well for sophisticated investors, as they create product that can fit various niches.

**FOX** The really valid point here is that once an issuer has reached a confidence point with investors around its business and its servicing strengths it is a long way along the path with that investor. When opportunities arise in areas like acquisition, there is a much better chance of cross-pollination when investors have this degree of comfort. They aren’t just buying asset risk – it is also servicer risk.

**Davison** *Is mezzanine financing from international investors a big contributor? The Australian market has been supportive but is limited in capacity and breadth.*

**CULHANE** To be honest, you can count these lenders on two hands – globally. We end up going back to the same lenders time and again, which is why it’s so important that we stick to our promises and make sure our deals perform. It is such a small community that one bad experience – even by accident – could cause a big problem for years to come.

**TUTTLE** Mezzanine funding in warehouses is also a fairly new technique. Before the crisis, the senior funder would typically lend all the way down the funding structure, typically down to our first-loss equity tranche.

The good news is that if you do a good job, the same investors show up in multiple transactions. Having good relationships with mezzanine debt providers is a key part of our global funding ambitions.



*“Mezzanine funding in warehouses is a fairly new technique. The good news is that, if you do a good job, the same investors show up in multiple transactions.”*

**PATRICK TUTTLE** PEPPER GROUP

profile. This includes financials as the starting point. But we also look very closely at business synergies and what we believe Resimac can add to an acquired business.

In the case of RHG, it was relatively easy because the product suite was such a perfect fit. The portfolio was absolutely ‘securitisation ready’ so there were funding advantages, and we were completely supported by our financial partners – especially National Australia Bank (NAB).

♦ **LEDINGHAM** The capital aspect was an important part of our due-diligence process. We looked at our equity base and to ensure we were adding assets to the balance sheet in a way that was optimally funded. As I mentioned earlier, this was done through common equity in the first instance – this was the best fit with our capital base at the time.

BOQ also dedicated quite a large team to due diligence on the Investec acquisition. From a treasury perspective, the real



task was to understand the funding, liquidity and risk profile into the future of the acquired business.

This means really understanding the assets – not just on a data level, but the current management of these assets, aspects of which may have been outsourced, and what can be brought back onto the balance sheet. It's a question of getting to grips with everything we are paying for, which goes as far as things like systems and staff. This is particularly important with a business like Investec, in which distribution is relationship-based.

**Davison** *Does it make a difference to the process if what is being explored is a 'whole-of-business' acquisition as opposed to taking on only some parts of an entity, for instance a discrete asset pool?*

♦ **LEDINGHAM** This was certainly relevant to the Investec acquisition. A significant part of the reason BOQ put such a large team on the deal was the fact that it was a whole-of-business acquisition. We had to look at various aspects, including treasury – funding and liquidity, risk management and, to some extent, capital – legal, credit and IT among others. Each of these had its own due-diligence needs. It was a very comprehensive process overall.

♦ **PLOUGHMAN** With the RHG acquisition, the unknown element was the servicing platform. We left this to one side as we didn't have sufficient information on RHG's servicing to make a call. This meant that the value of the acquisition had to stack up without servicing, which is a harder proposition. It did, however – and in the end being able to transition the acquired portfolio proved to be a value add of itself.

♦ **COX** The servicing component is critically important. There is work to do around the terms of servicing arrangements, and the approach will differ depending on whether servicing arrangements are migrating to the buyer, remaining with the existing servicer or transferring to another servicer entirely.

♦ **NEAGLE** Transition arrangements very much depend on the type of assets and the servicing arrangements in place at the time of acquisition. This includes whether the entity being purchased has an entirely independent and severable servicing capability or, for example, relies on a parent or the selling entity's general systems for some or all of its capability.

The extent of the transitional arrangements required will also depend on matters such as data and systems compatibility, whether there are any complicating factors such as co-branding arrangements, how the collections infrastructure is set up – including associated arrangements, which means things like direct debit arrangements – and the customer-messaging plan.

It is important that the transition comes with minimal impact to the consumer and a clear customer message. This is particularly so given some of the technicalities of these transitions can be necessary for the acquisition but may potentially be confusing for consumers, particularly in the retail space.

♦ **LEDINGHAM** One of our objectives in the Investec purchase was to maintain the business's distribution model without missing a beat for the end customers. We want to grow the book over time, but we have to remain aware that it is a relationship business.

**Davison** *From a legal perspective, how challenging is information exchange in an acquisition when three parties are involved – a seller, a nonbank buyer and the buyer's initial finance providers?*

♦ **COX** On the initial acquisition of a book, the seller will obviously come at it from the perspective of wanting to minimise the level of representation comfort it gives the buyer around the quality of the book being sold. The buyer, equally, is very interested in the level of representation comfort it receives – as are the acquisition financiers.

There is a potential disconnect between the buyer and its lenders on one hand and the seller on the other. We often need to manage what we might describe as 'basis risk' between the comfort given by the seller and the comfort the buyer needs to give to its financiers. If the seller is unwilling to provide the minimum requirements of the financiers, the buyer can bridge the gap in a few ways.

The first of these is a detailed spreadsheet, warranted as to accuracy by seller, containing data points about the loans being acquired. Alternatively, the buyer can obtain comfort for itself, and for their financiers, through its own due diligence.

**“VENDORS ARE COMING TO UNDERSTAND THAT THEY MAY NEED TO GIVE SOME SUPPORT TO FINANCING STRATEGIES, IN ORDER TO OBTAIN THE PRICING ADVANTAGES THAT PURCHASERS USING SECURITISATION TECHNOLOGY ARE OFTEN ABLE TO OFFER.”**

**ANNE-MARIE NEAGLE** KING & WOOD MALLESONS



## Cross-border concerns

AUSTRALIAN SECURITISERS HAVE BEEN ON THE ACQUISITION TRAIL INTERNATIONALLY. MAKING CROSS-BORDER PURCHASES COMES WITH AN ADDITIONAL SET OF CHALLENGES, WHICH CAN AFFECT THE VALUE PROPOSITION IF NOT DEFTLY HANDLED.

### **Davison** *What are the particular challenges involved in making cross-border acquisitions?*

**COX** The ability to transfer assets in and out of jurisdictions can vary depending on local laws. This may require funding structures to be set up locally to where the assets being funded sit. Any relevant withholding tax regime and the context of cross-border asset transfers or funding will also need to be considered.

**NEAGLE** There are also potential conflict-of-law issues depending on the matrix of jurisdictional connections, such as where the parties and the assets are located. Parties should be aware that the regulatory regimes, including for

example consumer credit or equivalent legislation, across jurisdictions may appear similar but can have important distinctions. Breaches can affect things in different ways. This includes in respect of the enforceability of the lending contract generally, or specific aspects of it such as fees.

**TUTTLE** There are a number of practicalities to be worked through – things like law firms. Our debt capital markets firm has historically been King & Wood Mallesons (KWM): it worked with us to set up our original master-trust programme here in Australia. Thankfully, KWM decided to establish a presence offshore and this has allowed us to continue working with the firm elsewhere in

the world – including in the UK, Hong Kong and mainland China.

**CULHANE** Both Pepper Group (Pepper) and KWM are heavily involved in structuring of warehouse and securitisation lines across the globe. Having this degree of continuity is extremely helpful. We want a global Pepper brand, with a similar experience wherever investors interact with us.

**PLOUGHMAN** We have acquired in New Zealand and the UK, and it is probably no surprise that we found New Zealand easier. It is easier from a timezone perspective, and in terms of the similarity of legal considerations.

Going further afield is more challenging – and, in general, the further away geographically, the harder it gets. We have tried to offset this to some extent by picking jurisdictions with legal environments similar to Australia, and we also funded our UK acquisition by going straight to securitisation – there was no bridge finance.

There is no set rule on this. But I think sellers in general appreciate this dimension to transactions, and understand that to achieve a clean and effective sale process it is not in their interests to be too limiting in the comfort they give potential buyers. This is not to say that comfort will always be sufficient to meet banks' requirements – there may still be extra steps needed on the part of the buyer.

♦ **NEAGLE** I agree that there is an increasing appreciation of this issue on the seller side – it's a trend I have seen in recent acquisitions. Ultimately, a key reason why a purchaser using securitisation technology for financing is able to put in a competitive bid may be because of the efficiencies it can generate through the use of this technology.

Vendors are coming to understand that they may need to give some support to financing strategies, in order to obtain the pricing advantages that purchasers using securitisation technology are often able to offer.

There are still limits on each side, in terms of how far each party is willing to go. But I am certainly seeing a greater appreciation of the source of competitive advantage in securitisation-financed bids, and of the need to come towards the purchaser's position to support the securitisation framework.

♦ **FOX** Despite the need for a compelling bid, in the main we have experienced alignment of interest between financiers and purchasers. NAB's role in this respect is as a senior

creditor to a special-purpose entity (SPE). As such, we place significant importance on the representation and warranty package provided by the vendor to the purchaser, and from there how this flows ultimately to the SPE for the benefit of secured creditors.

Remedies to the SPE and the operation of these are also important. This includes who provides remedies to the SPE and what is the look-through mechanism back to the vendor, whether there are duration limitations on some or all of the representations and warranties, and any fixed dollar claim caps.

Understanding assignability is critical, not just for financial close-funding arrangements but also for future capital-markets transactions. Understanding the position should we, or future investors, need to rely on these is important.

We also overlay other relevant acquisition-specific considerations. For example, the nature of receivables being purchased, and the seasoning profile and performance history of the receivables. Vendor-specific matters such as lending practices and transitional servicing arrangements are also relevant. The depth of the proposed due-diligence process by the prospective purchaser and the parties engaged in this process is also taken into account.

Having now been involved in a number of acquisitions in this sector, we find early engagement on these matters is key. It provides for constructive considerations and time to workshop solutions if needed.



**Davison** Presumably having an open communication channel with senior lenders is beneficial to nonbank buyers through the acquisition process itself?

♦ **TUTTLE** It certainly is. A high level of transparency puts discipline on us as the acquirer in a number of ways. Issues which we hadn't thought of can be raised in the credit processes of our senior lenders – like how we would specifically originate and underwrite granular consumer assets going forward.

These assets had historically been balance-sheet funded by the target company, so consideration needed to go into how we would originate these same consumer assets in such a way that they can ultimately be refinanced into securitisation markets.

It's good to be forced to think about issues like this while we are doing the acquisition, because there is no point thinking about them afterwards.

♦ **FOX** We don't view our involvement as a buy-and-hold process. We see it as an intermediation: we are helping our clients to grow their businesses over time, and to realise the full value of their purchases.

## EYE ON REFINANCING

**Davison** Most acquired securitisation portfolios will eventually be refinanced in the securitisation market, too. How does this knowledge influence the acquisition process itself?

♦ **COX** Part of the process should be ensuring the buyer and its banks have an eye to the future when they document the initial sale transaction – to ensure there is sufficient back-to-back comfort for public-market investors when it comes to refinancing.

♦ **NEAGLE** At the time of purchase there are often points for negotiation around the protection that can eventually be provided to public-market securitisation investors. For example, this may include whether the risk protections, if any, negotiated with the vendor will be provided to the purchaser only. If so, the purchaser will need to provide back-to-back protection to support a later public-market transaction.

Alternatively, risk protections can include an element of assignability for any future public term refinancing.

♦ **COX** An asset- or share-sale agreement will include the extent to which the seller is willing to allow the buyer to assign its rights against the seller in respect of representations and indemnities to future securitisation entities. Under normal circumstances, the buyer would expect to gain some ability to assign these rights.

**Davison** How easy is it to transition financing from the acquisition phase into the public market?

♦ **TUTTLE** The refinancing piece is crucial. Bank facilities have limited tenor – it could be anything from 12 months to three years – and we also have to prove to ourselves as well as the banks that there is a viable exit in terms of continuous refinancing into the debt capital markets. Without this, the banks won't have the confidence to make the senior lending in the first place – and we won't have the confidence to complete acquisitions.

♦ **FOX** The most important thing from our perspective is communication. A bank like NAB needs to understand its clients' current businesses when they are approaching acquisitions – strategic direction and the like – so we can build confidence internally around where the business is going.

♦ **TUTTLE** We are certainly aware of the need to communicate our strategy effectively to all management levels of our funding banks. They need to be able to get their credit approvals quickly, in order that we can continue to move through the sale process equally quickly. We can't afford to be left behind by another potential acquirer which may be able to rely on its own balance sheet without requiring third-party approvals.

♦ **COX** I think execution risk is quite low, because successful closing, execution and funding of bids from nonbanks is a relatively well-beaten path. All parties know what is expected of them and deliver to those expectations. Execution, despite some complexity in these transactions, has been very successful.

♦ **FOX** We also need the embedded skills in our own business around the securitisation product, including in terms of access to the capital markets. We have to be clear in our views around

**“THE CAPITAL ASPECT WAS AN IMPORTANT PART OF OUR DUE DILIGENCE PROCESS. WE LOOKED AT OUR EQUITY BASE AND NEEDED TO BE SURE THAT WE WERE ADDING ASSETS TO THE BALANCE SHEET IN A WAY THAT WAS OPTIMALLY FUNDED.”**

**TIM LEDINGHAM** BANK OF QUEENSLAND



liquidity available for various asset types, and being able to structure appropriately for this.

◆ **PLOUGHMAN** When we acquired RHG I was nervous about how quickly we would be able to refinance but our senior lender, NAB, was much more confident – I suspect because of its experience with Pepper’s acquisition of the GE mortgage book.

Bridge finance for any acquisition is key, but it is inevitably relatively short term and expensive. So naturally we wanted to refinance as quickly as possible – and our ability to do the first Avoca RMBS transaction of RHG assets within the first nine months of owning these assets was amazing. This kind of quick refinancing is a critical part of extracting value.

The mezzanine lenders come into warehouse financing for acquisition because, ultimately, they want the bonds that follow. They are really supportive of the securitisation, because it is this which produces the intended investment structure.

Being able to work with the NAB team was really helpful for us was. Because of their experience, we were able to go into the RHG acquisition with our eyes open – knowing what we needed to address. We also had some experience from our acquisitions in New Zealand and elsewhere, and of course you get better at everything with practice. So I think we would definitely feel more confident around the process of future acquisitions, which is one of the things which makes us keen to take advantage of good-value opportunities in future.

◆ **CULHANE** We have refinanced the New Zealand part of the GE Capital acquisition through private securitisation and have issued three securitisations of the prime GE Capital collateral in Australia. It’s an ongoing process.

◆ **TUTTLE** These refinancing transactions gave Pepper its first opportunity to issue US dollar RMBS tranches. NAB took us to the US market with a very innovative 2a7 funding structure, which opened up our programme to a whole new set of investors in the US money-market sector. We have since also taken our nonconforming deals to the US market, to extend liquidity among a broader group of international investors.

◆ **FOX** This speaks to my point about being confident in our own capabilities and read on the capital markets. With the 2a7, we needed to be very clear about what we were setting out to achieve – specifically, in this case, investor diversification – and then knowing how best to achieve that in a way which served the needs of both the issuer and investors.

**Davison** *Is identifying new investors a significant outcome of larger acquisitions?*

◆ **TUTTLE** It was important to us to open up other markets, given the significant reduction in the number of offshore investors active in the Australian market since the financial crisis. The US market has been very helpful for us as we have increased our origination volumes, year-on-year.

◆ **CULHANE** The GE Capital acquisition put Pepper on the map globally and, frankly, locally too. The fact we were able to digest a portfolio of this size made a lot of investors take notice of us for the first time.

## PROGRAMME SELECTION

**Davison** *Do issuers prefer to bring on board assets which can be additive to existing securitisation programmes or which can be – or already are – the basis of separate programmes?*

◆ **PLOUGHMAN** All of the above! We want bigger and we want more. Resimac has been a prime mortgage originator for 30 years, so when we went into the Bastille nonconforming programme we were nervous about investors’ level of comfort. But their attitude was ‘bring it on’.

We have been very well supported by our investors, including some who have supported every deal we have done. Their attitude to acquisitions has been to be happy that there are now more Resimac products they can buy.

The latest step has been the acquisition of assets, like the RHG portfolio, which are not Resimac originated. But our process and our promise to look after those assets in the ‘Resimac way’ have meant the investor support has carried across.

◆ **TUTTLE** I think there are economies of scale available in Australia. We have a very efficient back-office platform, which allows us to buy both mortgage and auto and equipment portfolios on an opportunistic basis – because we have capacity and operating leverage within our existing back-office operations to service them.

For example, we bought a small mortgage book from NAB in the past 18 months which was neatly migrated to our platform and can potentially be refinanced through our existing RMBS programme.



**“THERE IS A POTENTIAL DISCONNECT BETWEEN THE BUYER AND ITS LENDERS ON ONE HAND AND THE SELLER ON THE OTHER. WE OFTEN NEED TO MANAGE WHAT WE MIGHT DESCRIBE AS ‘BASIS RISK’ BETWEEN THE COMFORT GIVEN BY THE SELLER AND THE COMFORT THE BUYER NEEDS TO GIVE TO ITS FINANCIERS.”**

**BERKELEY COX** KING & WOOD MALLESONS



In Australia, as long as we are buying fairly familiar assets it is relatively simple to blend them with what we already own and thereby achieve demonstrable economies of scale.

♦ **CULHANE** It is a little different in Europe, where the issues are less to do with securitisation and more to do with servicing. The growth we have seen in Ireland, for instance, has given big economies of scale by allowing us to roll out our technology platform from Australia.

In the UK we have been able to deliver securitisation technology to mortgage originators as a servicer. This has allowed many UK securitisers to refinance their portfolios more successfully. Specifically, we have ended up as servicer on many UK loans which had become nonperforming during the financial crisis, but which we have helped get back on track. They have now become what we call ‘re-performing’ loans. Some have, more recently, been securitised.

**Davison** *How is the decision between refinancing as part of an established securitisation pool and from a discrete programme made?*

♦ **PLOUGHMAN** It’s certainly an active decision. For us, the decision to refinance the RHG portfolio out of the Avoca programme instead of Resimac Premier came down to the comparatively high quality of our standard prime portfolio.

We could have put the RHG assets into Premier, and we considered it – we could have significantly bulked up the programme and issued a much larger transaction. But the RHG book was not what would today be considered fully prime: it is 100 per cent mortgage insured, but it is largely a low-doc book.

I like the ability to issue into sweet spots of investor demand. Big deals are good, too, but we have to remember that there are, for instance, investors who will buy Premier but nothing else. If we start putting Avoca loans in this pool we will lose investors. On the other side, there are investors who are looking for yield and who love the maturity profile of the Avoca pool.

One of the good things about RHG is that it was a big enough book to issue discretely. But the decision isn’t set in stone. Whenever we look at financing we will always explore all the options – and we aren’t going to rule out ever putting RHG assets in with Resimac assets.

♦ **LEDINGHAM** As I mentioned earlier, the Investec assets securitised under the Impala programme are clearly different in nature from those in the BOQ REDS programme. Impala also has some aspects that are very high quality and appealing to investors: it has high-end customers and tends to be countercyclical in nature. So from this perspective it doesn’t necessarily make sense to comingle this book with REDS.

Having said this, we are still finalising the process of business and balance-sheet integration. When this is complete we will be better placed to look in more detail at how we fund the whole asset base in the most diverse way possible.

**Davison** *Does the funding of acquired books via separate securitisation programmes affect the synergies that can be achieved?*

♦ **PLOUGHMAN** RHG is in a separate trust. We run it in the same way as we run Premier, in Australia and New Zealand, or Bastille – it’s just another group of trusts that we manage. It didn’t need a separate treasury-management team, so there are still synergies on the funding side.

The synergies overall have been comprehensive. Our finance team does all the accounting, our securitisation team does all the funding, and our arrears team has revitalised the arrears management of the RHG book.

♦ **LEDINGHAM** One issue for us in this respect is that Impala deals have been relatively smaller – generally A\$200-300 million. We would like to see larger deals, in order to achieve the economies of scale which support the infrastructure of a standalone securitisation programme.

This doesn’t mean there is a lack of investor support for Impala assets – quite the contrary. On our investor roadshows in Australia, both for securitisation and senior-unsecured issuance, we are asked if and when Impala will return to issuance. Clearly there is support for the programme in the local market.

The challenge lies with our conviction that Impala is a different type of portfolio to REDS. No final decision has been made. But one option would be to warehouse Impala assets on balance sheet for now while we seek to scale up the business, then return to public securitisation via the standalone programme when the economies of scale justify it. The goal is potentially to have another avenue to market in time. ■

**“THE GE CAPITAL ACQUISITION PUT PEPPER ON THE MAP GLOBALLY AND, FRANKLY, LOCALLY TOO. THE FACT THAT WE WERE ABLE TO DIGEST A PORTFOLIO OF THIS SIZE MADE A LOT OF INVESTORS TAKE NOTICE OF US FOR THE FIRST TIME.”**

**MIKE CULHANE** PEPPER GROUP



# NEAR-PRIME RE-EMERGENCE

*Restrictive global regulation and progressively tightening lending criteria across the globe are leaving a growing number of mortgage borrowers on the fringe of banks' credit-lending models. In a project sponsored by **Commonwealth Bank**, ASJ examines the rise in importance of the specialist mortgage lender, by comparing the development of the market in Australia and the UK.*

BY HELEN CRAIG

**T**he extent to which the financial crisis and the subsequent regulatory response has constrained mortgage lending in Australia is significantly less than the paralysis of other markets, in particular the US and UK. Even so, the Australian regulator's reaction to the crisis was immediate and decisive: the National Consumer Credit Protection Act was implemented in 2010 and 2011.

In the UK, the financial crisis response saw existing mortgage-lending rules toughened up considerably. With more work required, the process was significantly more extended than in Australia: after a five-year lead time new lending criteria were introduced in the UK as part of the Mortgage Market Review, in April 2014.

Market participants in Australia point to the country's superior starting point on lending criteria (see feature on p12). Unlike most international jurisdictions, Australia's experience in 2008-09 was solely of a liquidity crisis rather than a liquidity and credit crisis.

Even so, mortgage borrowers in both Australia and the UK have experienced considerable changes since the start of the financial crisis as a result of adjustments in lender



*"Large banks are scaled up to lend in volume. They aren't easily able to deal with the unusual and this creates opportunities for specialist lenders like Pepper that don't rely on automated credit scoring."*

**PATRICK TUTTLE** PEPPER GROUP

behaviour and regulation. It is nonstandard borrowers – the self-employed, those borrowing into retirement or those with adverse credit histories – who have faced the greatest difficulties. In particular, bank lending appetite to nonstandard borrowers has eased significantly.

"What we have seen is banks generally tightening up in terms of some of the customers to whom they will lend," comments Rob Verlander, head of debt markets securitisation at Commonwealth Bank (CommBank) in Sydney.

The affected customers do not always match the picture of poor credit quality, subprime borrowers. "Near-prime" is a term used to describe a borrower who is effectively prime but for various reasons may fall out of the automated credit scoring used by larger lending institutions," Verlander explains.

This cements the need for the specialist lender, adds Justin Mineeff, Sydney-based executive director, debt markets securitisation at CommBank. "Specialist lenders take the time to analyse and understand the reasons why a borrower has fallen outside the particular criteria, and make a considered judgement around the probability of consistent good performance of that borrower going forward."

A number of firms see a similar opportunity set in Australia and the UK. Alistair Jeffery, executive chairman at Bluestone Group (Bluestone) in Cambridge, says when his firm started lending in Australia in 2000 it was mindful of its duty of care to customers, particularly those with past credit problems. "This is the approach that needs to be taken to lending in the UK, and it meshes neatly with the country's heavier regulatory landscape," he adds.

Jeffery suggests these experiences interlock, and notes the extent to which they are valuable for Bluestone's lending activities in both countries. "There are differences between the UK and Australian environments which make them difficult to compare on a like-for-like basis. But there are terrific opportunities for lenders in both jurisdictions – particularly in the UK, which makes it an especially interesting market for new entrants."

## DEFINING NEAR-PRIME

In Australia, the mortgage-lending market is still very much dominated by lenders' mortgage insurance (LMI) in the sense that credit criteria are generally set by insurers rather than bank lenders for loans of over 80 per cent loan-to-value. The insurers' LMI criteria are built into bank credit-scoring models.

"The models are quite rigid," Patrick Tuttle, co-group chief executive officer at Pepper Group (Pepper) in Sydney, tells ASJ. "Large banks are scaled up to lend in volume. They aren't easily able to deal with the unusual – and this creates opportunities for specialist lenders, like Pepper, which don't rely on automated credit scoring."

Similar credit criteria are used to assess a borrower's ability to repay loans

in the UK and Australia. All types of lenders in both countries shy away from habitual nonpayers or those with very recent mortgage arrears. The grey area is potential borrowers with relatively minor credit issues, who tend to fall out of the high-street bank sphere and into the specialist lenders' zone.

"We define borrowers with very minor credit issues as near-prime," reveals David Holmes, group chief operating officer at Pepper in Sydney. "These borrowers may have an aspect of adverse credit in their profiles, but such events have typically occurred 12-24 months prior to the date of application. If this had taken place less than 12 months before the application date we would view these borrowers as nonconforming."

Also falling into the specialist lenders' wheelhouse are self-employed and contract workers. In Australia these amount to 2.0 million – or 17.2 per cent – of the working population and in the UK 4.6 million or 15.0 per cent, according to Independent Contractors Australia and the UK's Office of National Statistics.

"It is very hard to get a loan as a self-employed borrower, whereas prior to the financial crisis this was an option," Tuttle reveals. "Particularly in the UK, the environment has become much stricter: if standard income evidence can't be provided it is hard to look at alternative means of verification."

Given both the UK and Australia now have numbers of people in self-employment at or near record highs, this gap in the market again creates significant opportunities for specialist lenders. The specifics of the UK's regulatory regime make the opportunity even larger, as the response to the crisis has been to apply much more restrictive lending rules (see box on p34).

### LIQUIDITY RETURNS

The UK was heavy with specialist mortgage lenders before the financial crisis. According to Richard Klemmer, chief executive officer at Pepper UK in London, the nonbank sector included more than 20 lenders in the near-prime and nonconforming space. The landscape has changed drastically. "There were a very small number of survivors – and some of the businesses that survived were repositioned to be only prime lenders," Klemmer confirms.

Market sources say liquidity is coming back into the UK market, having been largely absent in the specialist mortgage sector between 2009 and 2011. There is also associated capital-markets flow.

In terms of issuance volumes, the UK and Australia have a similar number of active origination programmes – there are five in the UK and four in Australia (see chart on this page).

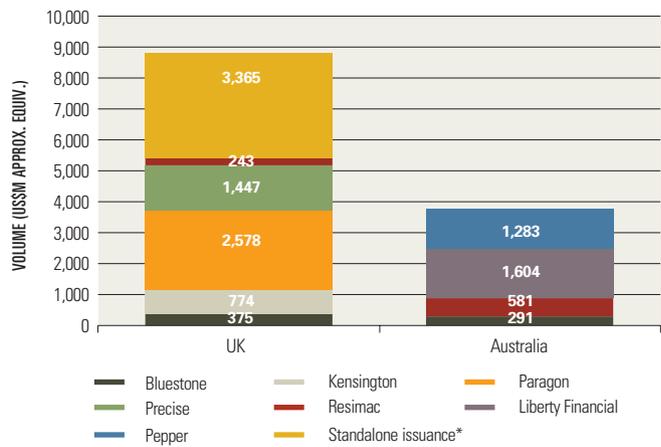
In fact, the two markets have shown a relatively similar

*"For quite some time the near-prime market has generated credit product with a spread that has been attractive for investors. This has led to significant demand for deals. In our prospective activity in the UK we envisage a similar appetite."*

**ROB VERLANDER** COMMONWEALTH BANK



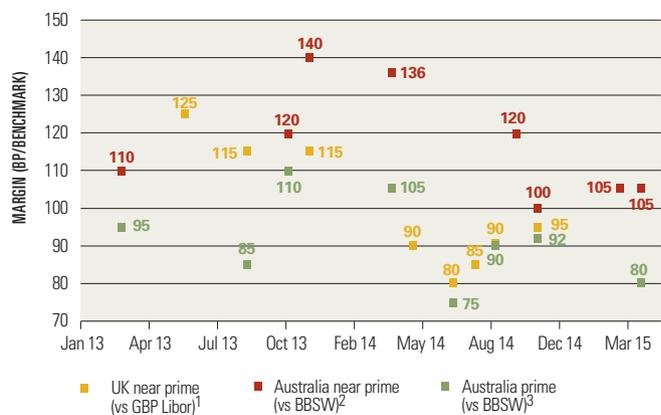
### NEAR-PRIME RMBS ISSUANCE VOLUMES JANUARY 2013 - APRIL 2015



\*Various recycled deals: portfolios that have traded on a loan basis, been bought by specialist funds and securitised.

SOURCE: FITCH RATINGS, KANGANEWS MAY 16 2015

### SELECTED AUSTRALIAN AND UK RMBS PRICING



<sup>1</sup> Average WAL 3.57 years <sup>2</sup> Average WAL 2.21 years <sup>3</sup> Average WAL 2.88 years

SOURCE: KANGANEWS, BLOOMBERG MAY 16 2015

level of activity in recent times. Excluding standalone – or recycled – deals, near-prime lenders have issued £3.4 billion (US\$5.3 billion) in the UK since the beginning of 2013, while in Australia the equivalent figure is A\$4.7 billion (US\$3.8 billion).

Bluestone has programmes in both Australia and the UK. The company's Sydney-based chief executive officer for Asia Pacific, Campbell Smyth, reveals that an opening up of capital markets in Australia was a catalyst for the issuer's return to

## Opportunity knocks

THE UK HAS SEEN A GROWING NUMBER OF PEOPLE BECOME NONSTANDARD BORROWERS IN THE POST-CRISIS YEARS. THIS HAS BEEN COMPOUNDED BY THE INTRODUCTION OF THE MORTGAGE MARKET REVIEW (MMR) WHICH HAS TIGHTENED STANDARDS IN THE UK CONSIDERABLY AND CONTRIBUTED TO A MORE CONSERVATIVE ENVIRONMENT IN WHICH TO LEND.

The MMR came into effect in April 2014 after a long consultation process. In fact, the work began with a discussion paper under the tenure of the now-defunct Financial Services Authority (FSA), in 2009.

Broadly, the main elements of the final rules are that lenders are responsible for assessing whether a customer can afford a loan, including by verification of the customer's income. In addition, lenders can only grant interest-only loans if there is a credible strategy for repaying the capital.

Kerion Ball, counsel at Ashurst, suggests the fact that lenders are now required to repeatedly assess borrowers' ability to repay is a clear differentiating factor around the UK's mortgage regulation.

"Lenders are expected proactively to ensure that throughout the life of the loan customers have credible repayment strategies," Ball tells ASJ. "For example, if there is an interest-rate rise lenders have to repeat some elements of the mortgage assessment – and look for early warning signs with

respect to customer payments and repayments."

The new rules required a complete overhaul of how lenders think about mortgage credit assessments. "The fundamental change brought by the MMR was the move from a traditional measurement of a borrower's ability to repay being a function of a multiple of their income and a debt-service ratio to a true affordability test," comments Richard Klemmer, Pepper UK's chief executive.

This includes a requirement that lenders apply a 3 per cent increase in the bank rate when assessing affordability of new loans, to allow for potential future increases in rates. Concerns that rate increases will affect mortgage holders with tracker mortgages have led the Financial Conduct Authority – the FSA's successor – to insist upon such types of stress test.

It was a significant challenge to get ready for the implementation of the MMR. "The challenge was felt as much among the mainstream banks as the specialist lenders," Klemmer adds.

### MMR versus NCCP

Australia's equivalent of the MMR is the National Consumer Credit Protection Act (NCCP). Market sources say Australia reached its standard of responsible lending in the run up to the NCCP's implementation in July 2010 and January 2011.

"The NCCP is not as prescriptive as the MMR in respect of responsible lending," Stanley Mok, senior associate at Ashurst, tells ASJ. "The NCCP provides that the lender has to take reasonable steps to verify a borrower's financial position and ability to repay the loan. It is not as stringent as the MMR in its rules around interest-only lending, and it does not expressly require the lender to stress test borrowers by taking into account interest-rate rises."

However, David Holmes, Pepper Group (Pepper)'s group chief operating officer, insists the MMR and the NCCP are more similar than might initially appear to be the case. He explains: "They both emphasise treating the customer fairly and ensuring customers are provided with the correct mortgage

issuance of Australian dollar residential mortgage-backed securities (RMBS) in December 2013, after nearly six years.

"A number of nonconformers have issued, albeit with some varied pools," Smyth tells ASJ. "Even so, there is no doubt that the market is open and this has enabled us to issue two deals, for more than A\$350 million total, in Australia over the last two years."



*"There are differences between the UK and Australian environments which make them difficult to compare on a like-for-like basis. But there are terrific opportunities for lenders in both jurisdictions."*

ALISTAIR JEFFERY BLUESTONE GROUP

### PERFORMANCE NOTED

Although the nonconforming sector remains niche within the overall Australian RMBS market, CommBank's Verlander notes the extent to which it has notched up strong performance over an extended period.

"For quite some time this market has generated credit product with a spread that has been attractive for investors,

and this has led to significant demand for deals," Verlander tells ASJ. "In our prospective activity in the UK we envisage a similar appetite."

The similar level of demand CommBank expects to see emerge for

product based on their circumstances and stated objectives. Low-doc loans, where there is little or no evidence of income provided, are obsolete in both jurisdictions.”

In the UK, borrowers who cannot provide the standard income evidence now required by all lenders are effectively disenfranchised from the market. In Australia, specialist lenders have developed alternative income verification methods acceptable under NCCP legislation.

“As long as a customer can validate the legitimacy of their source of income this type of lending is acceptable,” Patrick Tuttle, co-group chief executive officer at Pepper, reveals. “Pepper has developed an income verification product that looks at alternative income documentation such as 6-12 months of recent business bank or activity statements as evidence of cash flows. Unlike the MMR, the NCCP does not tightly define how borrowers provide evidence of income.”

According to Holmes, both the NCCP and MMR regulations have

been very beneficial. Customers’ circumstances are rigorously checked and their abilities to repay thoroughly examined. “This ensures customers are only advanced a loan based on what they can afford and, moreover, that they are provided with a product that best meets their needs,” Holmes explains.

Tuttle adds that the legislation has also helped weed out some of the more unwelcome elements of mortgage lending that existed before the crisis. “The new legislation has been constructive in Australia and the UK,” Tuttle argues. “There is a much higher standard of broker education. This is a very welcome development for an institution like Pepper, as around 60 per cent of our origination comes via mortgage brokers.”

#### Near-prime prospects

Even in the stricter environment of the UK, the market is now effectively functioning – despite new lending dipping when the MMR came into force while lenders made the most

of the transition period to get their practices and systems in place.

Within this fledgling environment, Ball sees clear opportunities for near-prime lenders. “Larger institutions are taking quite a conservative line to the implementation of MMR requirements,” he insists.

Peter McGuinness, chief executive officer at Bluestone Group’s capital-management division, also sees opportunities for near-prime specialists in the new assessment environment. “The MMR is putting pressure on credit-scoring techniques – with the UK regulator making it clear that lending requires a more intimate review of a borrower’s circumstances. The idea that you can just query a credit bureau, or rely on what a borrower tells you in terms of income and expenditure to suffice for serviceability, is long gone.”

Importantly for specialist lenders, McGuinness also claims: “The high-street banks do not have the infrastructure in place or the experience in niche lending to compete under the new regulatory backdrop.”

*“Lenders are expected proactively to ensure that throughout the life of the loan customers have credible repayment strategies. For example, if there is an interest-rate rise lenders have to repeat some elements of the mortgage assessment.”*

KERION BALL ASHURST



good-quality near-prime assets in the UK is partly driven by a tightening of prime and near-prime spreads in the UK in recent years.

Kerion Ball, London-based counsel at Ashurst, explains: “Investor appetite for yield has, in part, driven a tightening of prime and near-prime spreads in the UK in recent years. Prime lenders – which have access to alternate sources of funding such as deposits and central-bank funding – may be more focused on the costs of executing an RMBS than nonbank lenders in the near-prime market for which RMBS is an important source of funding and current spreads are comparatively favourable.”

Paragon Mortgages (Paragon) has been active in the niche buy-to-let space in the UK since 1997 – it has operated in this space exclusively since 2001 – and says it is currently the only UK financial institution whose core business is this kind of

lending. The firm believes spread compression can go still further despite the significant tightening already experienced. It points to a comparison between its own issuance and prime deal flow since November 2013 to illustrate the point (see table on p37).

John Harvey, Paragon’s Solihull-based head of structured finance, notes significant spread compression, but expects the gap to prime spreads will narrow even further as issuance conditions continue to improve.

He comments: “When we issued before the recession we were working on narrowing the difference between prime and nonconforming. It took some time, but by our PM15 RMBS in July 2007 our senior notes priced practically on top of a prime deal that was executed at the same time.”

Indeed, pricing data show that Australian dollar product offers greater compensation for investors: selected near-prime

## Playing catch up

FOR NEAR-PRIME LENDERS, THE MORE INFORMATION THAT CAN BE SOURCED ABOUT BORROWERS THE BETTER. REGIMES IN THE UK AND AUSTRALIA DIFFER, BUT MARKET PARTICIPANTS IN BOTH JURISDICTIONS ARE COALESCING AROUND A SINGLE FORM OF CREDIT REPORTING.

Australia has been one of the world's laggards in terms of implementing a positive credit-reporting regime. Traditionally, Australia's major banks – with their market-dominating positions – and to a lesser extent the government have been lukewarm on the concept of positive credit reporting.

Yet in March last year comprehensive credit reporting commenced in Australia under changes to the country's Privacy Act. Previously, personal credit files could only hold negative information on borrowers – for instance if they missed a credit card payment.

Comprehensive credit reporting changes the level of information that can be held on an individual's file. Under the new scenario an individual's credit history will also include positive credit information, such as if borrowers make a payment on time.

Despite the changes to the Privacy Act, comprehensive credit reporting is not yet mandatory under Australian legislation. This means while lenders are encouraged to participate they are not bound to do so – and market sources say larger lenders are in no rush to adopt the practice.

### UK example

In the UK, the positive-reporting regime has been in existence for some time, giving the benefit of significant historical data.

"In our review of the UK market we have seen that lenders use this data in a very proactive way," Justin Mineeff, executive director, debt markets securitisation at Commonwealth Bank, reveals.

He continues: "The main benefit of positive reporting is in origination – it is possible to make a better decision on whether to lend. But the additional benefit is that positive reporting can help a lender if it observes a borrower's situation has changed over time."

From an underwriting perspective, Richard Klemmer, chief executive officer at Pepper UK, is an advocate of the deeper and more comprehensive level of information that is available in the UK compared with Australia. "As a nonconforming lender, our role is to identify the risks in credit profiles that put borrowers outside the prime environment. Only once we have identified these can we accurately assess an individual's situation. The

more information we have to do this the better."

A positive reporting regime in Australia could benefit the consumer, too. "Positive credit reporting would enable us to become more granular around how we price our products," Patrick Tuttle, co-group chief executive officer at Pepper Group, tells ASJ. "Because we are somewhat blinded by negative reporting we have to request source documents from borrowers – such as bank, mortgage and credit card statements – which leads to an inefficient process. Under a positive credit-reporting regime the mortgage application process would be more streamlined for borrowers and would provide a greater depth of knowledge to lenders."

For the time being, Australia's big banks are being encouraged to opt in, and are being given time to do so. But Stanley Mok, senior associate at Ashurst in Sydney, reveals: "We understand that in 2017 there may be a government review of the take up of positive credit reporting. This is to ensure that sufficient banks are participating. If they aren't, participation may become mandatory."

and nonconforming primary bond pricing has narrowed – albeit marginally – since the beginning of 2013. But primary spreads on RMBS in the Australian market continue to be wider than their UK counterparts, even though Australian issuance is traditionally at a shorter weighted-average life (see chart on p33).

### A CROSS-SECTION OF APPETITE

The buyer base for securitised near-prime product in the UK crosses over into prime territory, Pepper UK's Klemmer explains. "Certain funds that have an appetite for asset-backed securities will look across the spectrum of the underlying asset class. These investors get comfortable with the individual portfolios, the originator and the sector, and will likely then buy prime and near-prime."

Demand also stretches offshore, especially into Europe. Paragon's Harvey tells ASJ demand was particularly robust for its PM22 RMBS, which contained a euro tranche. "This increased the investor base in Europe and also had an impact on the sterling investor base, which grew as a result. In fact, all tranches in this transaction were oversubscribed. Before the



*"Before the recession Paragon was issuing in sterling, euros and US dollars. I'm sure at the appropriate time and as deals grow in size we will start to issue in US dollars again."*

JOHN HARVEY PARAGON MORTGAGES

recession Paragon was issuing in sterling, euros and US dollars. I'm sure at the appropriate time, and as deals grow in size, we will start to issue in US dollars again."

Even so, Peter McGuinness, Cambridge-based chief executive of Bluestone Group's capital-management division, says investors are quite specific about underlying assets. This is why more than £2.1 billion of the £5.6 billion volume in the UK market since early 2013 has been raised via a variety of recycled deals. These are portfolios that have traded on a whole-loan basis, been bought by specialist funds, then securitised and put back out into capital markets.

"Investors want repeat issuance, a credible ability to call deals and strong servicing credentials. They are also cautious around one-off exits of legacy portfolios," says McGuinness. "They are looking for evidence that the current sponsor behind a deal has the intent and capability to return for further capital-markets issuance."

### PATHS TO ISSUANCE

Australian securitisation issuance traditionally comes from warehouses originated by a securitiser, which then make their way into primary bond markets. The UK also offers market access to portfolios that have entered run-off mode.

These portfolios emerged from the near wipeout of the specialist-lender heavy UK market, in which nonbank lenders were all but eradicated when, for the most part, they found themselves unable to fund their operations. Portfolios originated by such lenders were effectively put into structured run-off mode – hence they retained a number of the features of a regulated lending business that were easy to resuscitate.

Bluestone was able to enter the UK market after purchasing a legacy portfolio and a licensed mortgage platform, McGuinness reveals. "Our objective was to identify a well-managed mortgage platform, with capital-markets capabilities and contemporary Financial Conduct Authority permissions to originate and service residential mortgages."

Bluestone purchased a platform that was previously owned by Westdeutsche Landesbank in partnership with Macquarie Bank. The complete programme – including its 15 staff and portfolio under management of around £600 million – was auctioned, McGuinness explains. Other opportunities like this exist, he continues. "I

### PARAGON RMBS ISSUANCE COMPARITIVE SPREADS

ISSUE DATE	PARAGON ISSUE	LARGEST TRANCHE SPREAD (BP/LIBOR)	PRIME ISSUE	LARGEST TRANCHE SPREAD (BP/LIBOR)	DIFFERENTIAL (BP)
Nov 11	PM16	275	Gosforth/Arkle 2011-1	145	130
Oct 12	PM17	135	Gosforth 2012-2	47	88
Sep 13	PM18	115	Lanark 2013-1	45	70
Mar 14	PM19	85	Lanark 2014-1	40	45
Jul 14	PM20	68	Fosse 2014-1	40	28
Nov 14	PM21	80	Brass No.4	47	33
Mar 15	PM22	80	Fosse 2015-1	32	48

SOURCE: PARAGON MORTGAGES MAY 19 2015

wouldn't say the UK market is littered with them but there are a number of other platforms that were effectively put into hibernation and are now being invested in by new owners."

A number of Australian nonbank mortgage originators have taken strategic approaches to the acquisition of asset portfolios – including in offshore jurisdictions. These include nonperforming portfolios, those in run-off mode and others which have merely become non-core to their previous owners' business models (see roundtable discussion on p22).

The UK market is still working to re-establish itself in the post-crisis world, but sources insist the many moving parts are shifting in the right direction. In some ways the UK has attributes – in terms of credit-reporting information for instance – that give it more appeal than the Australian equivalent (see box on facing page).

"Structures are being modified in line with investor sentiment," Ashurst's Ball tells ASJ. "The market is still reasonably opportunistic, but repeat issuance is occurring. For instance, Precise Mortgages has issued more than £800 million of RMBS since December 2013."

The same characteristics exist in Australia. Most notable is the regularity by which nonbank issuers are able to access capital markets in the country. There are also opportunities for new securitisers – and for these to be repeat issuers. For instance, La Trobe Financial priced A\$102 million in its debut RMBS in March last year and launched a follow up this May.

"Issuers are able to access the Australian and UK markets on an ongoing and regular basis," CommBank's Verlander argues. "There is no doubt that specialist lenders have a role to play from both a lending and an origination perspective." ■

*"Specialist lenders take the time to analyse and understand the reasons why a borrower has fallen outside the particular criteria, and make a considered judgement around the probability of consistent good performance of that borrower going forward."*

JUSTIN MINEEFF COMMONWEALTH BANK



# DEMAND FOR RMBS HOLDS UP, DESPITE CONFIRMATION OF AOFM PORTFOLIO DIVESTMENT

*The news that the Australian Office of Financial Management (AOFM) has been directed to divest its remaining holdings of residential mortgage-backed securities (RMBS) does not appear to have caused any concern in the wider market. Indeed, the pricing of Australia's largest nonbank RMBS since the financial crisis immediately followed the announcement.*

BY HELEN CRAIG AND SAMANTHA MENZIES

**A** little over two years since the AOFM ceased investing in RMBS, the government debt-management agency announced on May 13 that it would be selling its residual portfolio of approximately A\$4.6 billion (US\$3.7 billion).

Under the divestment process the AOFM expects to sell A\$300-500 million – based on the total amortised value of the notes to be sold – of RMBS per month by auction, with the first sale scheduled to take place in June. The specific timing and securities to be offered will be announced at least a week before the auction, the AOFM confirms. It adds that the “auctions are unlikely to be held on the same date of each month...to avoid potential complications arising from ex-coupon periods”.

The AOFM has previously conducted a number of sales of its RMBS holdings, though the goal of previous sales has generally been to assist market price discovery rather than as part of a broader divestment strategy. These sales have

tended to be at the lower end of the planned volume range for the larger sell-down programme, and generally with several months between any divestments of A\$300 million or more (see chart on this page).

The latest announcement marks a strategy shift on the part of government, revealed as part of the 2015 federal budget. Budget papers say Australia's treasurer “has issued a direction for the remaining RMBS holdings to be gradually divested”.

## EXECUTION STRATEGY

While the AOFM itself is tight-lipped on how it plans to conduct the sell down, its announcement hints at a strategy mindful of not saturating a secondary securitisation market which does not historically transact large volume. The AOFM says it is “mindful of the potential for the divestment to [affect] the RMBS market with measures in place to ensure the treasurer is kept abreast of market conditions”.

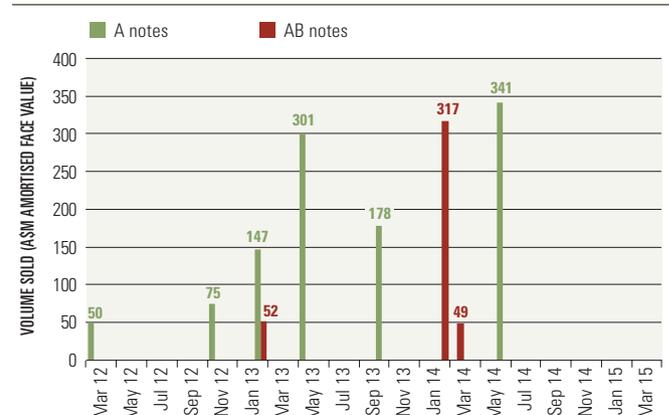
Indeed, market responsibility is stipulated in the treasurer's May 5 directive, which reads: “The AOFM should apply its discretion on the timing and sale volume to minimise potential market disruptions.”

The directive continues: “Following completion of a sale, the AOFM must publish the outcome of the sale, including the price, volume of securities sold in terms of original and amortised face values, estimated weighted-average lives [WALs] in years, and estimated traded margins in basis points.”

The mechanism by which the AOFM intends to execute the sales is consistent with the debt-management agency's declaration to be consistent and transparent, Martin Jacques, head of ABS strategy at Westpac Institutional Bank (Westpac) in Sydney, comments. “The monthly auction, the notice of which securities will be up for auction and the amount of each sale will give investors sufficient time to carry out credit work. This will attract the maximum number of buyers to each sale.”

This transparency reflects the way the AOFM has managed its RMBS portfolio from the outset, argues Stephen Maher,

## SECONDARY-MARKET SALES OF AOFM RMBS HOLDINGS



\* Not shown: the AOFM also sold A\$74 million of AB notes in March 2010

SOURCE: AUSTRALIAN OFFICE OF FINANCIAL MANAGEMENT MAY 20 2015

Sydney-based division director, head of debt markets research at Macquarie Bank (Macquarie). “The AOFM has always sought to extract maximum value out of its activity and in this particular instance

*“The AOFM has always sought to extract maximum value out of its activity and in this particular instance the value is in the ability to provide information to the market. The divestment activity will enable the AOFM to pinpoint the clearing price for assets.”*

**STEPHEN MAHER** MACQUARIE BANK



the value is in the ability to provide information to the market. The divestment activity will enable the AOFM to pinpoint the clearing price for assets which will, in turn, provide guidance on secondary- and also primary-market trading for at least the next 12 months.”

## ELEPHANT IN THE ROOM

Given the size of the portfolio – the agency invested a total of A\$15.5 billion over a period of nearly four years (see chart on this page) – the AOFM’s plans for its RMBS has always been looming over the market to some extent, especially following the *ad-hoc* sales, says Jacques. But he believes the new plan should in fact produce positive consequences.

“The divestment decision creates confidence in the market going forward,” Jacques explains. “We now know precisely what is going to happen to the portfolio and there is certainty that a large volume of assets won’t just be released into the market in an unstructured fashion.”

He adds: “After all, the AOFM dedicated five years to supporting the securitisation market with a view to fostering a sustainable, innovative market which was not reliant on government support. We think it is unlikely that the government would proceed with a policy that would undo all that hard work.”

An environment of generally robust securitisation market conditions means the AOFM’s decision to divest the remainder of its RMBS portfolio is less likely to have a negative impact. Jacques continues: “In 2014, securitised issuance volumes were

the highest since the financial crisis, there have been several new entrants into the RMBS market and – aside from a brief period of widening at the end of 2014 – spreads have been coming in steadily over the last couple of years.”

## MARKET VIEWS

Gary Sly, executive director, structured capital markets at ANZ in Sydney, says his bank’s expectation for spread direction is that levels may end up marginally different from its best-case scenarios as a result of the AOFM’s intentions. “We were expecting the emergence of a post-Easter RMBS pipeline to cause spreads to compress a little – in line with other markets – from their pre-Easter levels. But whether this compression will be of the same magnitude as we had previously expected may now be in question.”

Jacqui Fox, head of securitisation origination at National Australia Bank (NAB) in Melbourne, tells *ASJ* that there may be some initial concerns in the market around investor demand for paper, although this may be partly mitigated by the fact that the AOFM has always very carefully managed its RMBS programme.

“The programme is of reasonable size so there may be some risk that the divestments could put pressure on investor demand – although this should only affect a small number of accounts and not the broader market,” Fox comments. “Having said this, sufficient statements have been made to provide the market with confidence that the AOFM will continue to be sensitive to market conditions.”

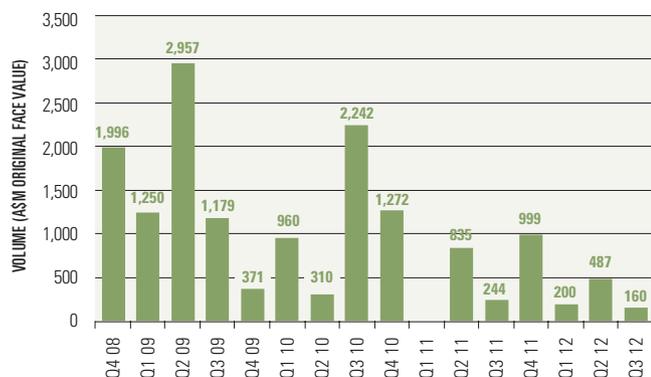
Other market participants appear to be broadly confident that the AOFM sales will be supportive of market development. They agree that the AOFM’s plans should not put pressure on investor demand for RMBS paper.

Phil Miall, head of credit research and strategy at QIC in Brisbane, explains: “The A\$4.6 billion current face value should be comfortably digestible for the market as the sales will take place subject to market conditions and on a gradual basis.”

In fact, because these parcels will be of a “readily digestible size”, Miall believes the additional supply could actually see RMBS spreads tighten somewhat. “The *modus operandi* for the previous AOFM sell downs has been that they have traded at fairly tight levels. On some occasions this has led to a tightening in the secondary market.”

He adds: “Additionally, the AOFM portfolio is of good quality, well-seasoned and of a size that we expect will attract

## AOFM INVESTMENTS IN RMBS



SOURCE: AUSTRALIAN OFFICE OF FINANCIAL MANAGEMENT MAY 20 2015

solid demand from both bank balance sheets and real-money investors.”

## PRICE DISCOVERY

Rob Verlander, head of debt markets securitisation at Commonwealth Bank in Sydney, says public information on the trading levels of existing RMBS paper can be quite difficult to come by. Hence he argues the AOFM’s divestment is positive for the market.

Verlander says: “There is a disconnect in size between the very large primary market and the smaller secondary market. To the extent that bids for the AOFM’s portfolio – for which there will presumably be price discovery around where paper is trading in the secondary market – can be seen, this is very positive.”

Secondary-market trading provides another source of primary-market price validation, Verlander adds. “There is an intense focus on primary-market deals but considerably less on secondary. To have ongoing secondary-market scrutiny of paper that investors own is undoubtedly a positive development for the market.”

Fox believes additional scrutiny on the secondary market as a result of the divestment is constructive, for both domestic



*“The AOFM portfolio is of good quality, well-seasoned and of a size that we expect will attract solid demand from both bank balance sheets and real-money investors.”*

PHIL MIALL QIC

and offshore investors, especially given the AOFM’s track record of having a supportive market approach. However, she also says: “The interaction between volume and what will ultimately move through the secondary market will be the eventual determination of whether or not this is constructive. And how these assets are divested is in the hands of the AOFM.”

Fox continues: “Often in periods of lulls we are looking to other issuance – for instance senior-unsecured deals – to give some line of sight around price points. Having regular consistency of price-point discovery during the divestment programme will be a positive market development.”

Verlander also points out that given the annual primary RMBS issuance levels of 2014 – of more than A\$30.0 billion according to *KangaNews* data – the market should have little difficulty absorbing an additional A\$4.6 billion of supply. “I would have thought this volume would be well within the capabilities of the securitisation market without negatively affecting price,” he argues.

Even so, Sly cautions that the AOFM’s target buyer universe may be limited – both by current market fundamentals and

the AOFM’s channels of distributing the bonds. He says: “At present the offshore investor base is not really participating in primary RMBS deals by virtue of swap costs, and I presume this cohort of investors is unlikely to participate in the AOFM’s parcels for the same reasons. The AOFM traditionally adopts a transparent approach in its dealings with the market. It will be the execution of the tenders, however, that will be key to investor participation.”

## NO LETUP IN ISSUANCE

Sly does not expect a halt in new RMBS issuance as a result of the AOFM’s RMBS divestment plans, though. “Investors continue to be constructive in the primary market, although of course only time will tell the real effects of this initiative. But in terms of the transactions that are currently making their way through the market we have not seen any reaction to the divestment.”

Other market participants agree that issuance patterns will likely continue unaffected, particularly in the context of observations around the composition of the AOFM’s portfolio.

“The AOFM portfolio is exceptionally well-seasoned with high levels of credit support,” Jacques says. “But the performance of some of the underlying assets is not

what you would expect from a primary-market issue: there are some transactions with levels of arrears above 3 per cent and some subordinated tranches that do not receive principal paydown for years. You’re comparing what in some cases is a six-year-old transaction with a clean, pristine pool which has been originated

and structured under contemporary structuring conventions and is priced at par.”

Fox says the differences between primary deals issued in the current environment and those making up the AOFM portfolio are also relevant. “One of the key elements is the change in the quantum of credit support provided in deals, and where they level out in time,” she explains. “Over the last few years, transactions have come to market with strong underlying credit characteristics and generally higher levels of credit support in terms of where they hold constant as the deal repays. While the AOFM portfolio is well seasoned, there is a trade-off in these features... I view hard credit support as a strong form of protection against declining property prices.”

Fox is also mindful of the composition of the AOFM’s portfolio. “A significant proportion of the exposure sits across four names. The good thing is those names tend to be well received in the market and these issuers have a range of available funding options to tap should they need. Nevertheless, the quantum of issuer-specific divestment and the timing of primary issuance would need to be considered

to ensure the objectives of both are well managed and to avoid oversupply on a particular name. I imagine these are things the AOFM will be considering, though.”

## UPTICK IN DEMAND

The immediate market response to the AOFM announcement does not appear to have been to turn against new issuance. Less than a week after the portfolio sale was revealed, Firstmac sold A\$1 billion in what was the largest RMBS priced by an Australian nonbank since before the financial crisis.

Firstmac cites an uptick in RMBS demand as the main factor behind its upsized volume. Distribution data provided by the borrower also reveal the support of a substantial domestic bid.

Firstmac Mortgage Funding Trust No.4 Series 2015-1 was increased from an indicative A\$500 million across eight tranches. The A\$600 million class A-1 note had pricing of 98 basis points over banks bills and weighted average life (WAL) of 2.9 years.

According to *KangaNews* data, the previous largest post-crisis AUD nonbank RMBS was a A\$750 million transaction from Credit Union Australia (CUA), which priced on February 13 this year. This deal, Series 2015-1 Harvey Trust, was also CUA's largest RMBS transaction since it issued the same volume in June 2007.

According to data provided by Firstmac, 22 investors participated in its latest RMBS – which had ANZ, J.P. Morgan, NAB and Westpac as its leads –

including 16 real-money accounts. The deal was predominantly sold locally: only two offshore investors participated, although these accounted for approximately 20 per cent of the book.

NAB's Fox reveals that while a couple of investors noted their views on the AOFM divestment during marketing of the Firstmac transaction, the anticipated impact in terms of whether this might have prevented them from participating in the transaction was, on the whole, neutral.

James Austin, chief financial officer at Firstmac in Brisbane, says the small number of offshore investors in the book was the most significant change from the issuer's previous deals. Each of Firstmac's 2014 RMBS transactions saw offshore investors account for approximately 50 per cent of paper sold.

“Foreign exchange rates blew out in December and have stayed wide since that time, meaning it has not been compelling for offshore investors to come into, and hedge, Australian dollars,” Austin comments.

However, he also explains that despite the drop off in offshore investor participation the Firstmac RMBS was supported by robust demand throughout its structure –

particularly in the junior and mezzanine structures – from domestic investors on a hunt for yield.

Austin also attributes part of the success of Firstmac's upsized RMBS to a change in its mortgage distribution to an online retailer, as well as its track record of “high credit quality and exceptional arrears performance”.

## ROBUST PIPELINE

According to *KangaNews* data, securitisation transaction volume in the year to mid-May has been solid: 17 deals priced for a combined volume of A\$13.2 billion excluding foreign-currency tranches. However, prior to Firstmac's return less than A\$2 billion of this volume had priced since mid-March.

Fears that the recent resurgence in issuance volume may be interrupted by the AOFM's asset sales appear unfounded, however. Market participants in general expect issuance to remain resilient to the asset sales and they say the Firstmac transaction appears to be the first sign of this coming through – though likely not the last.

Other issuers expect the AOFM's new direction to exert little pressure on future issuance plans. For instance, ING Bank Australia (ING Bank) has not yet issued an RMBS transaction in Australia so far in 2015, but it says the AOFM's planned RMBS

*“The AOFM dedicated five years to supporting the securitisation market with a view to fostering a sustainable, innovative market which was not reliant on government support. We think it is unlikely that the government would proceed with a policy that would undo all that hard work.”*

**MARTIN JACQUES** WESTPAC INSTITUTIONAL BANK



sales would not act as a deterrent to the issuer's return. Peter Casey, deputy treasurer at ING Bank in Sydney, confirms: “The AOFM appears to be planning to sell volumes equal to one small- to medium-sized deal per month. I don't foresee any negative impact on the market if it executes the sales this way.”

Assuming a 25 per cent paydown on the A\$4.6 billion RMBS portfolio and a one-year process to divest it, Macquarie's Maher agrees that A\$300-500 million per month sales volume is unlikely to put unnecessary stress on the market. “The monthly volume is unlikely to be large enough to create a negative impact but will be sufficient to provide guidance through lulls in issuance.”

Generally speaking, Casey says, he too expects minimal disruption of day-to-day market activity as a result of the sales, given the volumes the AOFM is looking to divest and the fact that it intends to do so on a monthly basis.

*This content first appeared at [www.kanganews.com](http://www.kanganews.com): the leading independent source of news and information on the Australian and New Zealand debt markets. ■*

# RESIMAC: THREE DECADES OF PROGRESS

The year 2015 marks the 30th anniversary of **Resimac's** foundation. In this time, the organisation has changed from a government-owned entity established to provide private-market financing to the public housing sector to today's role as a prominent player in the nonbank sector. **Warren McLeland**, Resimac's executive chairman, and **Mary Ploughman**, head of capital markets, discuss the current positioning and future strategy of the company.

**R**esimac navigated its way through the crisis amid significant industry consolidation. What strategy has the organisation undertaken over the five years since that period?

◆ **MCLELAND** We've always ensured that we maintain excess capacity in both our asset and liability platforms, in order that we are able to take advantage of opportunities. We're principally in the business to grow organically but, where market conditions allow, we have no issues in augmenting growth with acquisitions aligned with our enterprise strategy.

◆ **PLOUGHMAN** We have been rather successful in pursuing acquisitions by

regulating our M&A activities in line with our risk appetite and funding capabilities. We have closed in excess of A\$2 billion (US\$1.6 billion) in asset and company acquisitions over the last three years in the domestic, New Zealand and UK markets. All have been integrated into our servicing and funding platforms in a very timely manner.

Investors have responded very favourably as we've expanded our issuance programmes in a way which has given them more product to look at. Last year we were able to securitise acquired assets in Australia, New Zealand and the UK. The next step for Resimac is to expand into new asset classes.

**Speaking of Resimac's investor relations work, and specifically**

**its issuance programme – what advantages do you feel the firm has in funding terms?**

◆ **MCLELAND** Where we consider we differentiate ourselves from our competitors is our ability to understand and meet the expectations of our investors over the long term. We come at our business from the perspective of the investor being the ultimate client we wish to service, in conjunction with the retail borrowers at the front end.

◆ **PLOUGHMAN** A prime example of this is a trade on which we are currently working, for which we have spent time with investors from the outset to understand where their interests and sensitivities lie. We will then try to accommodate these through aspects of duration and credit nuances in our structure.

We also pride ourselves on the provision of deal information, before and after issuance. Resimac has always made loan-level data available and has fostered a transparent approach to providing detailed information and data to investors – based on the understanding that they are the ultimate funders of our business.

◆ **MCLELAND** We have always regarded securitisation and disintermediation as irreversible trends, and so the underlying merit of the financing method never changed even though the securitisation markets suffered during the credit crisis.

As the securitisation markets have begun to recover, we have had to modify our capital model to reflect the new requirements of regulators and investors. A lot of our efforts have been geared to expanding and diversifying our investor base and issuance jurisdictions.

We are seeing more instances of disintermediation in the capital markets. This includes alternative asset managers

*“It is quite clear that there will be noticeable regulatory changes to the requirements around the capital adequacy of banks and also increasing scrutiny on their mortgage portfolios. These could, ultimately, result in an increase to the mortgage pricing banks offer. On a selective basis, we may be able to realise a competitive advantage in a pricing sense.”*

WARREN MCLELAND

now becoming more directly involved throughout the broader aspects of our funding programmes, not just as buyers of bonds.

**Securitised markets are obviously very important to Resimac’s business model. Exactly how important would you say they are?**

◆ **MCLELAND** The securitisation markets are pivotal. We rely on wholesale credit markets as we don’t possess any retail deposit-funding sources. Everything we do within the business is geared towards supporting the funding model to ensure Resimac always has access to various forms of wholesale funding.

◆ **PLOUGHMAN** We have seen a raft of regulatory changes over the last five years, but because we are a smaller organisation we have been more dynamic in terms of our ability to respond, and therefore to continue to access global credit markets. While bank issuers are restricted by the Australian Prudential Regulation Authority, we have been able to modify our deal structures to accommodate regulatory and rating-agency changes over time.

Resimac has met all of its first-occurring call options, even during the crisis where our refinancing costs were materially higher. This has been exceptionally well received by investors, particularly our European- and US-based relationships.

◆ **MCLELAND** The honouring of our calls demonstrated our long-term and future commitment to the global funding programme. While there were limited European issuance opportunities at the time, we valued our investor relationships and we felt we had a need to respect them and to meet our obligations with regard to the maturity profiles of our bonds.

**How has asset performance been over the last five years?**

◆ **PLOUGHMAN** We have seen our book’s performance improve significantly, which reflects tighter underwriting standards introduced during the early days of the crisis. There



has also been significant consolidation in distribution channels, aided by a national regulatory and licensing regime that has resulted in higher standards among mortgage-industry participants.

We have also created a stronger model by vertically integrating our origination sources, and this has further enhanced asset quality. Resimac now owns an aggregation platform, with in excess of A\$12 billion in loans, and an online channel. Both of these have translated into a better-performing, diversified book.

◆ **MCLELAND** They have also given Resimac greater control over its revenue, as we no longer have to pay remuneration to third parties. Our ability to leverage our technology capabilities has been a real enabler of establishing and building these proprietary channels.

**How has Resimac’s investment in technology and systems benefited its growth aspirations?**

◆ **MCLELAND** Our proprietary asset-management platform is a core attribute of Resimac. We have continued to make significant capital investment in the platform, to ensure it meets the requirements of both the asset and liability side of the organisation.

Our primary objective with our systems is for them to be as flexible and scalable as possible in order to support growth aligned to strategy, while also offering efficiency and productivity

outcomes and comprehensive management information systems reporting.

◆ **PLOUGHMAN** Owning our platform enables us to respond to opportunities, in the market and in terms of product development, with a degree of control and governance we would not have if using third-party providers.

**Do you see any opportunities for Resimac in light of forthcoming regulatory changes facing the banking sector in Australia?**

◆ **MCLELAND** It is quite clear that there will be noticeable regulatory changes to the requirements around the capital adequacy of banks, and also increasing scrutiny on their mortgage portfolios. These could, ultimately, result in an increase to the mortgage pricing banks offer. On a selective basis, we may be able to realise a competitive advantage in a pricing sense.

**How do you see Resimac positioning itself over the next five years?**

◆ **MCLELAND** I think we’re at a fork in the road with respect to future positioning. The shareholders and board want to see Resimac’s footprint expanded in Australia while simultaneously looking at strategic opportunities offshore, where there are complementary operating environments that would allow us to replicate the Resimac business model across international jurisdictions. ■

# AUSTRALIAN FINANCE GROUP



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAME	AFG TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	PRIME RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	55%
NUMBER OF SECURITISATIONS ISSUED	3
TOTAL VOLUME ISSUED	A\$875M
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$568M

**A**ustralian Finance Group (AFG) is one of Australia's leading financial-services companies. Founded in 1994, AFG has grown to become one of the biggest mortgage-broking groups in Australia, with more than 2,300 AFG brokers distributing more than 1,400 mortgage products supplied by AFG's panel of more than 30 lenders. The AFG loan book currently sits at more than A\$100 billion, making it the largest Australian loan book outside the major banks.

AFG leverages its tier-one technology platform to proactively manage its relationship with lenders, brokers and customers. AFG commenced offering its own securitisable home loans in 2007. These home loans are funded by multiple warehouses and term transactions. ■

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# AMP BANK



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	PROGRESS TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	PRIME RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	28%
NUMBER OF SECURITISATIONS ISSUED	18
TOTAL VOLUME ISSUED	A\$16.0BN EQUIV.
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	72% DOMESTIC, 28% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$4.2BN EQUIV.

**A**MP is Australia and New Zealand's leading independent wealth-management company, with the largest financial advice network in the region. It provides financial advice, superannuation services for individuals and businesses, investment products, and income protection, disability and life insurance. AMP has A\$215 billion in assets under management and more than 5,400 employees.

AMP Bank is an Australian retail bank offering residential mortgages, deposits, transaction banking and self-managed superannuation fund products, with around 100,000 customers. AMP Bank distributes through brokers, AMP advisers, and direct to retail via phone and internet. ■

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# ANZ BANKING GROUP



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	KINGFISHER

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	INTERNAL (FOR RBA REPO PURPOSES)
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	ZERO
NUMBER OF SECURITISATIONS ISSUED*	4
TOTAL VOLUME ISSUED*	A\$4.45BN EQUIV.
TOTAL DOMESTIC VS OFFSHORE ISSUANCE*	24% DOMESTIC, 76% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES*	ZERO

\* Excluding internal securitisation transactions. The last public RMBS issued by ANZ was in 2004.

**A**NZ Banking Group (ANZ) is one of the four major banking groups headquartered in Australia. ANZ provides a broad range of banking and financial products and services to retail, small business, corporate and institutional clients in Australia, New Zealand and the Asia-Pacific region. The bank began its Australian operations in 1835, its New Zealand operations in 1840 and has been active in Asia since the 1960s.

ANZ is one of only a small number of banks globally which has maintained a double-A rating from all three main credit-rating agencies. It is a true global issuer with a wholesale funding portfolio which is well diversified by currency, product and tenor. ■

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# AUSWIDE BANK



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	WB TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	PRIME RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	64%
NUMBER OF SECURITISATIONS ISSUED	12
TOTAL VOLUME ISSUED	A\$3.4BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$505M

**A**uswide Bank has recently been rebranded from Wide Bay Australia. Auswide Bank is Australia's 10<sup>th</sup> Australian Securities Exchange-listed bank. It has total assets of close to A\$3 billion.

Auswide Bank offers retail and business banking services to its clients across Australia, and has 33 retail branches from Cairns in far north Queensland to Robina on the Gold Coast. Its reach extends throughout Australia via the third-party network.

Auswide Bank has Australian credit and financial-services licences issued by the Australian Securities and Investments Commission, and is an authorised deposit-taking institution supervised by the Australian Prudential Regulation Authority. ■

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# BANK OF QUEENSLAND



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAMES	REDS (RMBS), REDS EHP (ABS), IMPALA (ABS)

## USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	RMBS, ABS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION*	13%
NUMBER OF SECURITISATIONS ISSUED	37
TOTAL VOLUME ISSUED	A\$21.6BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	APPROX. 91% DOMESTIC, 9% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	APPROX. A\$4.2BN

**B**ank of Queensland (BOQ) is a public company incorporated with limited liability under the laws of Australia. BOQ is domiciled in Australia, listed on the Australian Securities Exchange, is regulated by the Australian Prudential Regulation Authority as an authorised deposit-taking institution, and has total assets under management of A\$47.9 billion.

BOQ's loans under management total A\$39.7 billion, including housing lending of A\$27.3 billion, commercial lending of A\$8.0 billion, leasing of A\$4.0 billion and consumer lending of A\$300 million – reflecting the bank's focus on well-secured housing and SME lending. ■

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# BLUESTONE GROUP



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAMES	SAPPHIRE, EMERALD

## USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	RMBS, REVERSE MORTGAGE
WHOLESALE FUNDING VOLUME	A\$699.5M
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	79%
NUMBER OF SECURITISATIONS ISSUED	20
TOTAL VOLUME ISSUED	A\$6.1BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	94% DOMESTIC, 6% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$523M

**B**luestone Group (Bluestone) is a dynamic financial-services business with more than 250 employees, and operations in Australasia and Europe. The business is backed by Macquarie Bank and LDC, the UK's largest mid-market private-equity house.

In 2000, Bluestone began originating mortgages in the Australian market. In 2013, Bluestone recommenced mortgage origination and issued its first securitisation since 2007. With vast experience in the nonconforming mortgage space, Bluestone is excited to offer its mortgage products to the retail market and continue its issuance of RMBS. ■

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# COMMONWEALTH BANK OF AUSTRALIA



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	MEDALLION TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESale FUNDING SOURCED VIA SECURITISATION	5%
NUMBER OF SECURITISATIONS ISSUED	20
TOTAL VOLUME ISSUED	A\$52.5BN
OUTSTANDING VOLUME OF RMBS	A\$14.6BN

**C**ommonwealth Bank of Australia (CBA) is Australia's leading provider of integrated financial services including retail, premium, business and institutional banking, funds management, superannuation, insurance, investment and share-broking products and services.

The bank's approach to wholesale funding is to remain diversified across markets and to maintain a degree of flexibility in terms of timing of transactions. Wholesale funding is complemented by securitisation issues through the Medallion programme. ■

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# CREDIT UNION AUSTRALIA



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	HARVEY TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESale FUNDING SOURCED VIA SECURITISATION	70%
NUMBER OF SECURITISATIONS ISSUED	11
TOTAL VOLUME ISSUED	A\$6.3BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$1.7BN

**C**redit Union Australia (CUA) has a long and proud history providing banking and financial services to Australians. CUA is Australia's largest customer-owned financial institution with nationwide representation through more than 70 branches in Queensland, New South Wales, Victoria and Western Australia.

CUA is an authorised deposit-taking institution and is regulated by the Australian Prudential Regulation Authority. ■

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# FIRSTMAC



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAME	FIRSTMAC MORTGAGE FUNDING TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESale FUNDING SOURCED VIA SECURITISATION	75%
NUMBER OF SECURITISATIONS ISSUED	30
TOTAL VOLUME ISSUED	A\$14.8BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	88% DOMESTIC, 12% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$4.6BN

**F**irstmac is a leading nonbank originator of prime residential home loans. Loans are sourced through the company's own online retail business – [www.loans.com.au](http://www.loans.com.au) – and through an Australia-wide network of third-party brokers and mortgage managers. The company is headquartered in Brisbane and has offices in Sydney and Melbourne.

Firstmac has been a regular issuer of RMBS in the Australian domestic and offshore markets since 2003. ■

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# FLEXIGROUP



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAME	FLEXI ABS TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	ABS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	43%
NUMBER OF SECURITISATIONS ISSUED	7
TOTAL VOLUME ISSUED	A\$1.4BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	>90% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$418M

All data as at May 31 2015.

**A**n ASX200-listed Australian public company, FlexiGroup is a leading provider of vendor and retail point-of-sale finance. FlexiGroup's diversified business streams offer a broad set of products and services that can adapt to the specific needs of vendor partners. These include leasing, interest-free cards, no-interest payment plans, cheque guarantee and lay-by. ■

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# HERITAGE BANK



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	HBS TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	PRIME RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	45%
NUMBER OF SECURITISATIONS ISSUED	11 PUBLIC DEALS, 3 AUD WAREHOUSE ARRANGEMENTS, 1 AUD INTERNAL SECURITISATION ARRANGEMENT, 1 AUD PRIVATE DEAL
TOTAL VOLUME ISSUED	APPROX. A\$6.1BN EQUIV.
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	APPROX. 59% DOMESTIC, 41% OFFSHORE *
OUTSTANDING VOLUME OF SECURITISED ISSUES	APPROX. A\$610M EQUIV.

\* By original issuance. Only domestic issues remain.

**H**eritage Bank (Heritage) is Australia's largest mutual bank, with approximately A\$8.3 billion in total consolidated assets as at December 31 2014. It is a public company, limited by shares and guarantee, which operates as a mutual organisation. The mutual business structure is an integral component of Heritage's operating philosophy.

Heritage is an authorised deposit-taking institution, regulated by the Australian Prudential Regulation Authority. ■

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# IMB



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	ILLAWARRA TRUST

## USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	RMBS, CMBS (SMALL TICKET)
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	72%
NUMBER OF SECURITISATIONS ISSUED	6 RMBS, 3 CMBS
TOTAL VOLUME ISSUED	A\$3.3BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$977M

**IMB** is one of Australia's largest building societies, with assets of more than A\$4.8 billion and approximately 178,000 members. Established in 1880, it is also the longest-standing building society in New South Wales.

IMB is regulated by the Australian Prudential Regulation Authority and the Australian Securities and Investments Commission. It is a member of the Customer-Owned Banking Association – an independent organisation representing building societies, credit unions and mutual banks. ■

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## ING BANK (AUSTRALIA)



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	IDOL TRUST

### USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	24%
NUMBER OF SECURITISATIONS ISSUED	8
TOTAL VOLUME ISSUED	A\$7.5BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	96% DOMESTIC, 4% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$4.5BN

**ING DIRECT** – the trading name of ING Bank (Australia) – is a branchless retail bank. It is part of the world’s leading direct savings bank and is wholly owned by ING Group. It offers products in retail mortgages, transactional banking, retail savings, specialised commercial-property markets and retail superannuation.

With more than A\$32 billion in retail deposits, A\$38 billion in mortgages and 1.5 million customers, ING DIRECT is one of the largest home lenders in Australia. ■

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## LA TROBE FINANCIAL



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAME	LA TROBE FINANCIAL CAPITAL MARKETS TRUST

### USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	<10%
NUMBER OF SECURITISATIONS ISSUED	1
TOTAL VOLUME ISSUED	A\$102M
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$75M

**La Trobe Financial** is a leading credit specialist focused on residential and commercial assets. It offers credit solutions for prime and alternate income-verification consumers who mainstream providers do not accommodate. Formed in 1952, La Trobe Financial has lent more than A\$10 billion of mortgage loans for institutional and retail clients. It has offices in Melbourne, Sydney and Shanghai.

La Trobe Financial undertook its initial RMBS offering in 2014 and subsequent issues are planned. ■

*Editor’s note: the company issued its second RMBS deal in May 2015, for A\$250 million. The data above do not include this transaction.*

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## LIBERTY FINANCIAL



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAME	LIBERTY TRUST

### USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	ABS, CMBS, RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	66%
NUMBER OF SECURITISATIONS ISSUED	34
TOTAL VOLUME ISSUED	A\$13BN+
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	84% DOMESTIC, 16% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	APPROX. A\$2.1BN

All data as at April 30 2015.

**Liberty Financial** is one of Australasia’s leading speciality finance groups. Its businesses include residential and commercial mortgages, motor-vehicle finance, investments and insurance in Australia and New Zealand. It employs approximately 200 professionals and has issued more than A\$13 billion in domestic and international capital markets.

Since 1997, Liberty has helped more than 150,000 customers achieve their financial goals. Liberty is one of the few lenders in Australasia with an unblemished capital-markets record. No rating downgrades or charge-offs have ever been experienced by its originated securities or programmes. ■

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# MACQUARIE GROUP



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAMES	SMART, PUMA

**M**acquarie Securitisation (manager of the PUMA RMBS programme) and Macquarie Securities Management (manager of the SMART auto- and equipment-lease programme) are wholly owned subsidiaries of Macquarie Bank, which is a regulated authorised deposit-taking institution and part of the Macquarie Group.

## Macquarie Group

Macquarie Group is a global financial-services provider. It acts primarily as an investment intermediary for institutional, corporate and retail clients and counterparties around the world. Founded in 1969, Macquarie Group employs more than 14,000 people in 28 countries. At March 31 2015, Macquarie Group had assets under management of A\$486 billion.

Macquarie Group is listed in Australia and is regulated by the Australian Prudential Regulation Authority as the owner of Macquarie Bank, an authorised deposit taker. ■

## SMART PROGRAMME

### USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	ABS
NUMBER OF SECURITISATIONS ISSUED	27
TOTAL VOLUME ISSUED	A\$20BN EQUIV.
CURRENCIES ON ISSUE	USD, AUD, GBP, EUR
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$7BN EQUIV.

## PUMA PROGRAMME

### USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
NUMBER OF SECURITISATIONS ISSUED	57
TOTAL VOLUME ISSUED	A\$51BN EQUIV.
CURRENCIES ON ISSUE	USD, AUD, EUR
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$10BN EQUIV.

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ME



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAMES	MAXIS, SMHL

USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
NUMBER OF SECURITISATIONS ISSUED*	44
TOTAL VOLUME ISSUED	A\$42BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	A\$25.5BN, US\$10.4BN, €2.2BN
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$4.4BN

\*Combined Members Equity Bank Limited and historical mortgage-origination business.

**M**E, which rebranded from ME Bank in May 2015, was created in 1999. Its origins date back to 1994 when, as an initiative of the Australian Council of Trade Unions, National Mutual launched Super Member Home Loans.

ME is owned by 30 industry superannuation funds. It has historically provided low-cost home loans and banking products to members of industry super funds and unions. Recently, ME opened its product offering to the broader Australian population while still offering member benefits to its traditional base.

ME's goal is to offer banking services, with products that are simple, straightforward and offer value for money to working Australians. ■

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MYSTATE BANK



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	CONQUEST TRUST

USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
WHOLESALE FUNDING VOLUME	A\$1.4BN
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	49%
NUMBER OF SECURITISATIONS ISSUED	5
TOTAL VOLUME ISSUED	A\$1.2BN*
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$667M

\*Includes the joint securitisation undertaken by MyState and Queenslanders Credit Union in 2007.

**M**yState Bank (MyState) along with The Rock Building Society (Rock) are wholly owned authorised deposit-taking institution subsidiaries of MyState Limited – a non-operating holding company approved by the Australian Prudential Regulation Authority and listed on the Australian Securities Exchange.

MyState operates predominantly in Tasmania (10 branches) and provides services to 117,000 customers, state-wide. Rock operates in Central Queensland (seven branches) to 40,000 customers, as well as providing lending services throughout Australia via indirect channels. ■

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NATIONAL  
AUSTRALIA BANK



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	NATIONAL RMBS TRUST

USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	RMBS, ABS
NUMBER OF SECURITISATIONS ISSUED	4 EXTERNAL RMBS, 1 EXTERNAL ABS
TOTAL VOLUME ISSUED	APPROX. A\$14BN (EXCLUDES RETAINED DEALS)
TOTAL DOMESTIC ISSUES	7
TOTAL CROSS-BORDER TRANCHES	7

**N**ational Australia Bank (NAB) is a financial-services organisation with more than 12.7 million customers and 42,000 people, operating more than 1,700 stores and business-banking centres globally. Its financial-services franchises in Australia are complemented by businesses in New Zealand, Asia, the UK and US.

Each of NAB's brands is uniquely positioned, but built on a common commitment to provide customers with quality products and services, fair fees and charges, and relationships built on the principles of help, guidance and advice.

NAB's activities include banking, credit- and access-card facilities, leasing, housing and general finance, international banking, investment banking, wealth and funds management, life insurance, and custodian, trustee and nominee services. ■

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# PEOPLE'S CHOICE CREDIT UNION



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	LIGHT TRUST

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	29%
NUMBER OF SECURITISATIONS ISSUED	4
TOTAL VOLUME ISSUED	A\$1.6BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	100% DOMESTIC
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$488M

**P**eople's Choice Credit Union (People's Choice) is Australia's second-largest credit union, with approximately A\$8 billion of total assets under advice and management. People's Choice has 345,000 members serviced through branches in South Australia, the Northern Territory, Victoria, Western Australia and the Australian Capital Territory.

Australian Central Credit Union, trading as People's Choice, is an authorised deposit-taking institution, is subject to prudential supervision under Australia's Banking Act and is regulated by the Australian Prudential Regulatory Authority. ■

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# PEPPER



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAMES	PEPPER RESIDENTIAL SECURITIES (PRS), PEPPER PRIME

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
NUMBER OF SECURITISATIONS ISSUED	13 PRS (4 OUTSTANDING, 9 CALLED), 4 PEPPER PRIME (4 OUTSTANDING)
TOTAL VOLUME ISSUED	A\$5.9BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	90% DOMESTIC, 10% OFFSHORE*
OUTSTANDING VOLUME OF SECURITIES ISSUED	A\$1.93BN, US\$282M

\* Two issues in the Pepper Prime series and one issue in the PRS series have included a USD 2a7 tranche, with the balance of the notes in AUD.

**E**stablished in 2001, Pepper is a leading Australian diversified financial-services group, with businesses in Australasia and Europe encompassing lending, third-party loan servicing and corporate real-estate advisory. Pepper has been a leading nonconforming residential-mortgage lender for more than a decade and has expanded to also offer prime residential mortgages and auto and equipment leasing.

Pepper is a highly rated third-party servicer and asset manager across a range of asset classes, including residential and commercial mortgages, auto loans, equipment leases, personal loans and unsecured small-business loans. ■

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# RESIMAC



AUSTRALIAN ADI	NO
SECURITISATION PROGRAMME NAMES	RESIMAC PREMIER, RESIMAC BASTILLE, RESIMAC AVOCA, RESIMAC VERSAILLES, RESIMAC UK

## USE OF SECURITISATION

TYPES OF SECURITISATION ISSUED	RMBS, NIM BOND
WHOLESALE FUNDING VOLUME FY15	A\$5.0BN
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	64%
NUMBER OF SECURITISATIONS ISSUED	34
TOTAL VOLUME ISSUED	A\$17.7BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	52% DOMESTIC, 48% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$3.2BN

**R**esimac was formed as a nonbank lender in 1985. It offers a suite of prime- and specialist-lending products tailored to the residential market, sourced from a distribution network of online and direct B-2-C proprietary channels, aggregators, mortgage managers and retail sources. Resimac is Australian-owned and also has operations in New Zealand.

Resimac was the first Australian RMBS issuer, in 1988. Since then it has issued more than A\$17 billion equivalent in 34 domestic and offshore issues. Resimac's capital-markets activities are core to its enterprise strategy and it remains one of the most prolific Australian nonbank issuers. ■

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## SUNCORP GROUP



AUSTRALIAN ADI	YES
SECURITISATION PROGRAMME NAME	APOLLO

## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION	17%
NUMBER OF SECURITISATIONS ISSUED	20
TOTAL VOLUME ISSUED	A\$22.53BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE	78% DOMESTIC, 22% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	A\$3.95BN, €101.5M

\* Based on notes only.

**S**uncorp Group is a unique, diversified financial-services group with well-known businesses in general insurance, banking and life. Suncorp Group is a top-15 Australian Securities Exchange-listed company with assets of A\$94 billion. It has around 14,500 employees and relationships with approximately nine million customers. Suncorp Bank is Australia's fifth-largest bank and Australia's largest regional bank. ■

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## WESTPAC BANKING CORPORATION



AUSTRALIAN ADI	YES
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**W**estpac Banking Corporation (Westpac) is Australia's second-largest banking organisation and one of the largest banking organisations in New Zealand. The bank provides a broad range of banking and financial services in these markets, including retail, business and institutional banking, and wealth-management services.

As at September 30 2014, Westpac had total assets of A\$770 billion. Westpac's ordinary shares and certain other securities are quoted on the Australian Securities Exchange and, as at September 30 2014, its market capitalisation was A\$100 billion. ■

## RMBS PROGRAMME

SECURITISATION PROGRAMME NAMES	WESTPAC SECURITISATION TRUST (WST), CRUSADE RMBS
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## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	RMBS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION <sup>1</sup>	5%
NUMBER OF SECURITISATIONS ISSUED	41
TOTAL VOLUME ISSUED <sup>2</sup>	APPROX. A\$76.4BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE <sup>3</sup>	73% DOMESTIC, 27% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	APPROX. A\$12.0BN

<sup>1</sup> Includes RMBS and ABS.

<sup>2</sup> Approx. 52% Crusade RMBS, 48% WST RMBS.

<sup>3</sup> Based on issues currently outstanding.

## ABS PROGRAMME

SECURITISATION PROGRAMME NAMES	CRUSADE ABS, BELLA TRUST
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## USE OF SECURITISATION

TYPE OF SECURITISATION ISSUED	ABS
PROPORTION OF OUTSTANDING WHOLESALE FUNDING SOURCED VIA SECURITISATION <sup>1</sup>	5%
NUMBER OF SECURITISATIONS ISSUED	13
TOTAL VOLUME ISSUED <sup>2</sup>	APPROX. A\$9.2BN
TOTAL DOMESTIC VS OFFSHORE ISSUANCE <sup>3</sup>	87% DOMESTIC, 13% OFFSHORE
OUTSTANDING VOLUME OF SECURITISED ISSUES	APPROX. A\$2.5BN

<sup>1</sup> Includes RMBS and ABS.

<sup>2</sup> Approx. 56% Crusade ABS, 44% Bella ABS.

<sup>3</sup> Based on issues currently outstanding.

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# ASF EDUCATION DATES

## Fundamentals

25 AUGUST 2015  
*Sydney*

19 FEBRUARY 2016  
*Melbourne*

25 MAY 2016  
*Sydney*

## Professionals

6 AUGUST 2015  
*Auckland*

10 SEPTEMBER 2015  
*Sydney*

15 MARCH 2016  
*Melbourne*

3 MAY 2016  
*Sydney*

## Refreshed

21 JULY 2015  
*Sydney*

21 AUGUST 2015  
*Melbourne*

1 APRIL 2016  
*Sydney*

## Applied

29 OCTOBER 2015  
*Sydney*

16 JUNE 2016  
*Melbourne*

## Special Workshop – APS120

3 JUNE 2016  
*Melbourne*

10 JUNE 2016  
*Sydney*

24 JUNE 2016  
*Sydney*



Detailed course information and registration  
are available on our website:  
[www.securitisation.com.au](http://www.securitisation.com.au)



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Bank

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