**FSUG response to the Commission's targeted consultation "on the functioning of the EU securitisation framework"**

FSUG focuses on this question, as the most relevant in terms of the scope of FSUG work:

**Chapter 2, "Impact on SMEs":**

(...)

**2.2. How can securitisation support access to finance for SMEs?**

**Text of the submission:**

The FSUG is concerned that expectations for securitisation to contribute to the funding of European SMEs is overstated and unrealistic. At the end of 2023, SME loans accounted for only ca. 15% of total asset-backed securities (ABSs) outstanding in the EU (excluding Collateralised Loan Obligations, CLOs). Even in the US, the market routinely referred to by promoters of securitisation as the reference standard, securitised SME loans represent only a small fraction of the total issue volume, and a large part of that issuance consists of loans granted under federal guarantees, similar to agency-backed mortgage securities.

There are good factual reasons: in reality, the securitisation of corporate loans has only limited potential to mobilise additional funding for corporations, especially SMEs. Inherent practical limitations constrain the size and relevance of this market: (i) SMEs often have little to no viable collateral, these assets often have little or no alternative use, and are difficult and time-consuming to liquidate; (ii) loan sizes and financial terms vary significantly – even within the category of ‘micro-, small- and medium-sized enterprises’ (as per Art. 2(3.a.i.) of DelReg 2019/1851), which affects the granularity of the pool; (iii) contractual terms and conditions are tailored largely to individual creditors' requirements. In many Member States it is, and will continue to be, challenging for banks to construct pools of loans for securitisation which are at once (i) sufficiently homogeneous – not only in terms of the STS homogeneity factors of Art. 2(8) SECR and Art. 2(3) of DelReg 2019/1851 (type of obligor and jurisdiction) but in terms of the principal criteria which ultimately determine investors' credit quality and cash flow characteristics of the loans; and (ii) sufficiently large to achieve the necessary economies of scale and absorb the inherent costs of the securitisation structure (which are significant, especially in the case of a traditional – ‘true sale’ or ‘cash’ securitisation).

As with securitisation in general, these underlying economics favour large banks capable of mobilising portfolios of the required size at the expense of smaller competitors. SME lending is traditionally a domain in which smaller banks are able to compete with their larger peers based on local knowledge, long-standing relationships, and a more granular understanding of borrowers' businesses and risk profiles. This business model, which contributes significantly to the diversity and resilience of the EU banking sector, would likely come under significant competitive pressure as a result.

The FSUG doubts that securitisation could substitute for the lack of capital market integration. Rather to the contrary, promoting securitisation would merely increase the reliance of European corporates on debt funding, which renders them more fragile in cyclical downturns, and especially on bank debt. By promoting securitisation, instead of tackling the admittedly complex but ultimately indispensable integration of EU primary debt and equity capital markets, the dependence of the EU corporate sector on banks would only become even more entrenched. The FSUG considers there are more streamlined ways to improve access to finance for European SMEs, than relaxing the current securitisation regime. In order to improve access to funding for SMEs the EU should instead review and expand existing programmes, such as the EIF's equity funding facilities, invest in the development of interconnected and interoperable European trading and settlement infrastructures for securities, and harmonise legal frameworks to facilitate and incentivise cross-border investment within the EU. Public support, where available, should be channelled directly towards the real economy instead of subsidising (‘de- risking’) the banking sector.

It should also be noted, in this context, that banks are not obliged to redeploy the so-called ‘freed-up capital’ towards granting new loans, i.e. new (additional) SME financing. In recent years, many EU banks, especially large, listed groups, have announced generous distributions to investors, with payout ratios often well over 50%, even though market conditions for new lending were favourable (high net interest margins and fee income); hence, the ‘additionality’ issue. There are simply too many aspects that influence the banking sector's ‘appetite’ for lending, first and foremost the phase of economic expansion and contraction, as well as perceived external risks. The observed relationship between securitisation and lending is too tenuous to support a simple causal argument that easing securitisation standards would strongly kick-start SME lending.

As pointed out by some NGOs which are present in FSUG, ‘securitisation severs the relationship between lenders and borrowers. Removing the link between lender and borrower redefines the way banking is conducted (the ‘originate to distribute’ model), creates a different set of incentives inside financial institutions, and moves large blocks of credit exposures out of the regulated banking sector. That may slowly lead to a deterioration of the European banking landscape. Features of the European ‘relationship banking’ model, such as forbearance and loan restructuring, become more difficult to apply and the enforcement of collateral more likely’[[1]](#footnote-1).

This becomes particularly relevant when residential mortgages or other retail exposures, such as credit card receivables or consumer loans, are securitised. These categories accounted for ca. 70% of all securitisations in the EU (excluding CLOs) outstanding at the end of 2023. Residential mortgage-backed securities (MBS) alone accounted for ca. 60% of the total.

Introduction of a third party (the Special Purpose Vehicle, SPV) hugely affects the relationship between the lender and borrower. Even if the originating bank continues to service the loan on behalf of the SPV, it no longer has the autonomy to amend or modify the loan agreement, e.g. extend its maturity or grant a payment holiday. The SPV, in turn, has little room for manoeuvre and little incentive, given its commitments to investors, e.g. to grant forbearance. As a result, lenders are more likely to call in the loan and seize their collateral, a step that is already very painful when applied to a typical consumer or SME loan, and potentially traumatic when applied to a mortgage.

In many EU member states, mortgage loans are refinanced using alternative instruments, especially covered bonds. Covered bonds constitute a large, liquid, and highly effective market. They contribute significantly to the availability of affordable mortgages in many EU member states. Their specific design (over-collateralisation, dual-recourse) makes them a high-quality asset in great demand by international investors. Built-in limits on leveraging the underlying collateral also act as a brake on the systemic build-up of leverage in the property market. **Promoting securitisation, e.g. by relaxing the prudential requirements for financial institutions in this market could interfere with the market for covered bonds and may eventually inflict more harm on existing, well-functioning segments of the CMU than it contributes in terms of benefits.**

There is still some room how, other conditions equal, securitisation can still play a role in SME financing. However, that would have to involve steps beyond the scope of the existing EU's securitisation framework *per se* (and beyond the scope of this consultation). Securitisation should be considered primarily as a complementary financing option for asset classes that do not readily lend themselves to being refinanced by other, more cost-efficient means which pose fewer risks, especially for retail borrowers and taxpayers). To the extent that certain categories of secured corporate loans (e.g. automotive or equipment leasing) are sufficiently homogeneous and granular, and especially if they could be readily pooled across EU jurisdictions, securitisation could make a useful, albeit limited contribution to the CMU.

Last, but not least, the FSUG wants to remind that those who forget the lessons of the past are condemned to repeat it. Securitisation of sub-prime mortgages was a key-driver of the last global financial crisis. Many of those securitised-assets received the best possible ratings from rating agencies, fuelling excessive risk-taking from banks and investors. Securitization can be very risky if there is little knowledge about the quality of the assets that are included in the securitized products. Investors need to know the quality of the underlying assets in a securitized product so they can accurately assess the risk they are taking on.

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1. <https://www.finance-watch.org/wp-content/uploads/2024/10/20241004_Introduction-to-Securitisation-Structures-regulation-and-market-for-asset-backed-securities-in-the-EU.pdf> [↑](#footnote-ref-1)