Impact of securitisations and loan transfers activity on M4 lending

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This article aims to explain how and where securitisations and loan transfers impact on monetary data. Details of securitisations and transfers of loans, to individuals, can be found in Table A5.7 of this publication.

Background

Securitisations and loan transfers

A securitisation occurs when a portfolio of loans, similar in purpose and usually of high credit quality, are grouped together and transferred either to a special purpose vehicle (SPV[1]) or a non-resident company which funds the purchase through the issue of bonds. SPVs are specifically set up by institutions to purchase their loan portfolios. Non-resident institutions are usually associated with the seller, which may itself be a non-resident SPV.

When a portfolio of loans is acquired or disposed of by an institution in the UK, without the issue of bonds to fund the purchase, it is known as a loan transfer for statistical purposes.

The majority of loan transfers and securitisations are either loans secured on dwellings or are credit card debt, although commercial mortgage securitisations also take place. Securitisations and loan transfers pass on the monetary and legal interest in all the loans within the portfolio to the purchaser.

Why do institutions securitise portfolios?

Securitisations take place for a variety of reasons, such as:

- risk management;
- to provide an additional source of funding;
- to free up economic and regulatory capital;
- balance sheet management; and
- profit maximisation.

When a portfolio is acquired by an institution the assets are moved from the originator's balance sheet to the purchaser's balance sheet. The purchasing institution may acquire the portfolio to gain exposure to a new area of business or to increase market share.

[1] An organisation constructed with a limited purpose or life. In relation to securitisations it means the entity set up to hold the legal rights over the assets transferred to it by the originator.

Effects on published data

Impact on M4 Lending data

M4 lending[2] is sterling lending by monetary and financial institutions (MFIs) - in the UK these are banks and building societies only - to the M4 private sector[3]. Securitisations and loan transfers within M4 lending, unless between MFIs (SPVs are not MFIs), will reduce the stock of lending outstanding, and the monthly change in amount outstanding, the flow, by the amount of loans securitised. To give a clearer picture of M4 lending, aggregate series are calculated which exclude the effects of securitisations by adding the securitised amount back to the stock of lending and to the flows. The sectoral analysis of M4 lending, in Table A4.3 of this publication, are adjusted for the effects of securitisations.

When loans are sold to non-residents the lending stock is not adjusted - it is permanently reduced, as the asset has left the UK. Flows are adjusted to remove the effect from the monthly data as the lending has not been repaid by the borrower.

Adjusting M4 Lending for securitisation effects has a large cumulative impact on the stock as well as monthly effects on the flows and growth rates. Table 1 shows the differences between the adjusted and unadjusted series for October 2004.

Table 1: M4 lending for October 2004[(a)]

£ billions	Amount outstanding	Change on month	Annual growth
M4 Lending	1,495	8.1	11.4%
M4 Lending (excl effects of securitisations)	1,597	8.0	12.9%

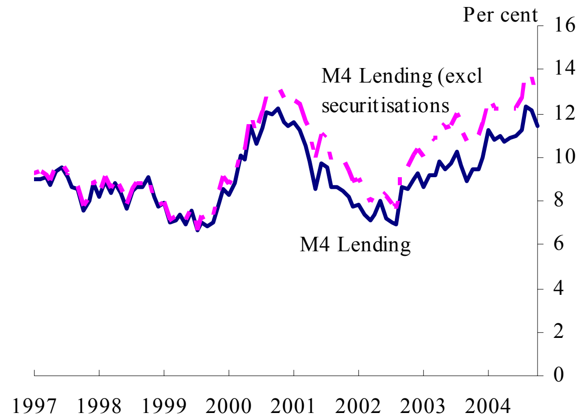
(a) Data are seasonally adjusted

[2] These data are published in the M4 statistical releases and are available on the Statistical Interactive Database via the Bank of England website www.bankofengland,co,uk/mfsd/iadb.

[3] M4 private sector consists of all UK residents other than the public sector and MFIs.

As securitisations and loan transfers have become more popular the annual growth rates between the unadjusted and adjusted series have diverged (see Chart A) with the adjusted series being up to 1.7 percentage points higher than unadjusted series in some months.

Chart A: Annual growth in M4 lending[(a)]



(a) Data are seasonally adjusted.

Further details on securitisations and loan transfers

Securitisations and loan transfers to UK resident institutions are recorded within total lending to individuals[4] – a measure that includes lending by a broader set of institutions than the banks and building societies that account for M4 lending – in Table A5.7, but sales to non-residents are only footnoted in Tables A4 and A5 as they happen. Portfolios of loans transferred between banks, between building societies or between other specialist lenders, are not shown in Table A5.7 as they net out within the respective sectors.

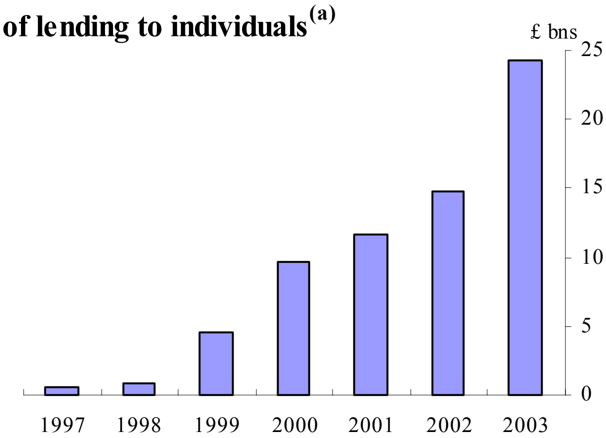
Portfolios can also be de-securitised[5]. In this case securitised loans will move from the SPV back to the original lender; for example when bonds are redeemed – the value of the securitised portfolio must be in line with the value of the bonds in issuance. De-securitisations are usually very small, normally below £50 million; these amounts are also included in the series on Table A5.7. Other additional small transactions between lenders and their SPV recorded in Table A5.7, are known as top-ups and draw-downs. They take place quite frequently in order to keep the value of the securitised portfolio in line with the value of the bond issuance. A top-up will transpire to replace any loans that are repaid, while a draw down will remove any additional lending made to securitised accounts.

[4] Includes lending to individuals by other specialist lenders (SPVs, non-bank UK credit grantors and specialist mortgage lenders); retailers (consumer credit only); and other credit granters such as central and local government, public corporations, insurance companies and pension funds; as well as banks and building societies.

[5] 'De-securitisations' happen when all, or part, of a securitisation is brought back onto the balance sheet of the institution it originally left.

Securitisations have increased significantly in the past five years. The value of securitisations has increased from £0.6bn in 1997 to £24.4bn in 2003. The strong increase is probably the result of factors such as higher consumer borrowing and strong demand for these types of securities by investors. Chart B shows the annual volume of net securitisations and loan transfers of mortgages and consumer credit by banks.

Chart B: Banks' securitisation\loan transfers of lending to individuals[(a)]



(a) These data are consistent with Table A5.7 and therefore exclude transfers to non-residents; banks' balance sheets are reduced by the amounts shown.

Impact on Total Lending to Individuals

As mentioned previously total lending to individuals is a measure that includes lending by a broader set of institutions than the banks and building societies that contribute to M4 lending. Series are not produced excluding securitisations for total lending to individuals as the other specialist lenders sector includes all SPVs based in the UK as well as other institutions lending to individuals who are not MFIs. Again, the only securitisations and loan transfers that are lost from the amounts outstanding are those which are sold to non-residents (the effects of this are adjusted out of the flows).

Statistical treatment of covered bonds

Secured lending associated with Covered bonds, held by institutions which do not form part of the MFI sector, had been consolidated on banks' balance sheets, however, in future these data will be reported on an unconsolidated basis and the secured lending will appear in the other specialist lenders sector. The movement of secured assets will be shown in Table A5.7 in future.