Securitised debt markets in Asia are poised for growth, but challenges remain

Securitised debt has, at best, played a supporting role in Asia over the past decade or so. No sooner did issuers and investors begin to embrace the product than it met an unexpected hurdle that took the wind out of its sails. By Colin Chen, head of structured debt solutions, treasury & markets, DBS Bank

Asian securitised debt experienced a steep reduction in the issuance volumes during and immediately after the financial crisis, with a large number of active investors withdrawing from or reducing their appetite for such investments. But we are now seeing the appetite for securitised debt return in the fast-growing Asian economies – a trend also seen in the global securitised debt markets. The growth in Asia, however, is perhaps currently limited by the number of active investors. In Asia (ex-Japan), a significant majority of both cross-border securitised debt and local currency securitised debt issuances continue to be placed with banks or bank-sponsored vehicles, funds and insurance companies. The emergence of investors, both Asian and global, may be a reflection of the state of global liquidity. The lack of highly rated, quality assets will only encourage investors to consider the merits of Asian securitised debt, especially from a relative value return perspective.

The major securitised debt markets in Asia-Pacific comprise Australia, Japan, South Korea, India, Singapore, Taiwan and Thailand, and includes both offshore and onshore local currency domestic markets. Markets in Indonesia and the Philippines have been stirring as well, with domestic transactions being worked on or recently closed. With Asia's growing economies and increased requirements for new growth capital, these trends are likely to continue in the medium term despite headwinds from the debt crisis in Europe, political uncertainties in the Middle East and natural disasters across the globe.

Given the nature of the global financial markets, Asia is no different from the European and US markets in terms of having to cope with ongoing changes in the regulatory landscape. Many Asian countries continue to be in different phases of regulatory development and implementation, with each of them dealing with country-specific concerns of inflation, asset bubbles and interest rates, as well as being in the process of aligning themselves with global regulatory initiatives and reform.

Colin Chen

Notwithstanding the regulatory landscape, central banks around the world continue to recognise the importance of a robust securitised debt market with adequate transparency and disclosure measures in place. Securitisation therefore continues to receive the support of regulators under the new Basel framework.

While the regulatory risks and measures continue to evolve, none of these measures will likely impact the quality of the underlying collateral pool. Contrary to popular perception, during the course of the financial crisis and the period immediately after, there was in fact very little deterioration in the quality of the supporting collateral for Asian securitised debt.

Source: Shutterstock/HenryHo

The performance of Asian securitised transactions immediately preceding the financial crisis has remained stable across most asset classes. There were no material downgrades in ratings levels for Asian securitised debt that could be attributed to underlying collateral performance during this period.

Despite spikes in the delinquency rates at the peak of the financial crisis, the underlying transactions' performance returned to normal levels within the year. This was due to the crisis' limited impact on unemployment rates and the region's strong economic recovery.

The ratings stability for securitised debt can be attributed to the fact that most Asian securitised debt is collateralised by consumer assets. They have also benefited from lower unemployment rates coupled with high economic growth rates from the Asian (ex-Japan) economies. These have helped contribute to the stable performance levels, especially compared to the US and European markets – which suffered from sustained declines in housing markets, concerns about refinancing needs for commercial mortgage-backed securities (CMBSs), high unemployment and increased sovereign debt concerns.

The underlying asset classes of securitised debt have also shifted in the aftermath of the financial crisis. We now see transactions that are less exotic and more vanilla. Common asset classes now include residential mortgages loans, credit cards and auto loans, although these asset classes differ geographically. For example, South Korean markets are dominated by offshore and local currency credit card, auto loan asset-backed security (ABS) and residential mortgage loan transactions, while India has an active local currency securitisation market, with commercial vehicles, construction equipment and residential mortgages being common underlying asset categories. In Singapore, the securitised debt market is mostly CMBSs with increasing consumer ABS issuances.

We have also observed interest in the securitisation of accounts or trade receivables and equipment lease receivables, as these institutions seek to optimise their capital and risk management.

With Asian securitised debt in particular, investments are in their most basic form. Investors purchase those with exposure to underlying performance indicators of Asian growth, namely consumer consumption – as in consumer finance receivables and trade and equipment lease receivables. This also reflects the manufacturing and export bias as well as the sustained construction boom in Asia.

New asset classes have been introduced in the region, including covered bonds and covered bond-like transactions. New Zealand and South Korea have already taken the first steps in that direction with the launch of their transactions. In the meantime, potential issuers in other jurisdictions continue to explore options in this area.

We expect this market to continue on a sharp growth trajectory, and high interest to remain in this asset category. With impending Basel III regulations, this asset class is likely to have a positive impact on the issuing banks' funding and liquidity profiles, as well as on asset liability management. In addition, we also expect issuers and investors to retain a high level of interest in cashflow collateralised loan obligations and expect to see more market activity in the area.

As global financial markets adjust to the introduction of new regulatory reforms, reliance on alternative sources of capital raisings and risk management tools will continue to increase. This supports the notion that there will be a revival in the Asian securitised debt markets. Only time will tell if this will finally lead to the growth of securitised debt in Asia.

Colin Chen
Head of Structured Debt Solutions, Treasury & Markets
colinchen@dbs.com
+65 6223 0978