

Securitisation versus Bank Loans

Abstract:

Today, the world of finance is becoming more complex than ever before. For instance, the rapid evolution of capital markets in recent years has shown an outstanding interest for moving to new areas of innovative finance. In contrast to the traditional ways of finance, banking system domination, as it was in the 1970s, is becoming critical especially for loans facilities.

This paper discusses the securitisation issue in comparison with bank loans. The asset backed securitisation (ABS) constitutes a real challenge that banks have to face. This situation obliges banks either to succeed in restructuring their activities and to adopt the new instruments emerging from the market, or to stay away from the development and the sustainability in the market.

**Dr. BOURAS Ahmed
BOUDAH Abdeldjalil**
Faculté des sciences
économiques et sciences de
gestion
Université Mentouri-
Constantine
(Algérie)

ملخص

يشهد عالم المال في الوقت الحاضر تعقيدا كبيرا من حيث النشاط والأدوات المستخدمة لم يعرف له مثيل من قبل. فالطور السريع الملاحظ في السنوات الأخيرة على مستوى أسواق رؤوس الأموال قد أبرز وبشكل ملفت للانتباه التوجه الجديد نحو مجالات التمويل المبتكرة والجديدة. على العكس من هذا، فإن الهيمنة البنكية في مجال منح القروض التي شهدتها فترة السبعينيات قد أصبحت عرضة لانتقادات حادة ومحرجة. فالمقال يتناول بالدراسة مقارنة موضوع عملية التوريق (أو التخليق)، باعتبارها تقنية حديثة في مجال التمويل، بإحدى آليات التمويل التقليدية والمتعلقة بمنح القروض. ويقصد بالتوريق، تحويل الأصول المالية غير السائلة المتمثلة في القروض طويلة الأجل إلى أوراق قابلة للتداول في سوق الأوراق المالية. فمثل هذا الإجراء، بالنسبة للبنوك، يعني تحد كبير يستوجب بالضرورة التكيف مع الوضع الجديد، من خلال إعادة النظر في النشاط القائم، أو الخروج النهائي عن كل أشكال النمو واستمرارية البقاء في السوق.

I- Introduction

The introduction of asset backed securitisation in this study is seen to be crucial. The question of securitisation is of vital importance because it holds significant implications that are explained by the ability to meet regulated capital requirements, reducing the cost of funds, and risks that can be managed.

Historically speaking, the birth of securitisation was first identified in the United States last century, at the beginning of the 1980s. Until the mid 1980s securitisation was considered to be only a U.S. phenomenon. However, studies run by [David M. W. Harvey, 1991] (1) and recently by others (2), showed that the United Kingdom has been considered as the leader within the European Community framework in implementing securitisation. This new way of development in financing is still a debatable issue under the European Community rules since securitisation's characteristics might not be well suited to the regulation of financial systems in Europe as it is in the USA.

Flourishing the idea of securitisation beyond the United States borders was as a result of benefits of such innovative mean that has proved its usefulness within financial service providers. Thus, the use of

the asset backed securitisation has been concentrated in financing short terms capital requirements, where working capital is concerned in a way that securitisation can be used in financing accounts receivables. By means of securitisation option a low cost funds can be achieved by packaging homogenous receivables for sales to investors, including banks, via the capital market.

As a matter of fact, the asset backed securitisation can be broken into three main different types : 1- real estates loans (residential mortgages), 2- consumer receivables which, in turn, are divided into long term consumer receivables (e.g. manufactured housing contracts) and short term consumer receivables (e.g. automobile loans, credit cards loans, and computer leases). 3- The third type of securitisation is called commercial and industrial (C&I) loan securities.

Until 1985 securitisation, particularly in the U.S. markets, was being applied to mortgage assets and consumer receivables. The application of securitisation on the non mortgage assets started after that period where in nowadays the securitisation of commercial and industrial loans is still in its embryonic stage compared with the securitisation of other types that are related to financial assets.

Last but not least, it can be said that studies run by [Edward Gardener, 1987] (3), [Gary J.Kopff and Jeremy Lent,1988] (4) , [Juan M. Ocampo [1989](5), have treated the securitisation subject in relation to the bank's role that concerned with financing firms in the market place. Further, these studies have analysed the erosion of banks' role where there should be a need for an emergency evolution to absorb the innovative means of securitisation by reshaping banks structure to the development of financial markets.

II-Bank loans approach

Among the traditional ways of bank financing are, of course, those concerned with loans that are usually being given on the basis of collateral. Generally speaking, collateral can be considered as an important role in bank lending, as evidenced by the fact that nearly 70 per cent of all commercial and industrial loans in the USA are made on a secured basis (6). Therefore, a further explanation on this particular point of approach is thought to be crucial since it illustrates the difficulties that often banks face in providing loans to firms. Indeed, the use of collateral within the traditional bank's activities is now receiving considerable attention in the literature of financial contracting.

It is argued, [Besanko and Thakor, 1987] (7), and [Chan and Kanatas, 1985] (8), that the relationship between collateral and borrower quality is based on the fact that safer borrowers are more likely to pledge collateral. However, this theoretical view has been contrasted to the banking view which shows that riskier borrowers are more likely to pledge collateral. An essential difference between the two opinions is that the former one is usually based on private information that risk can only be known by borrowers, whereas the latter view concentrates on observed risk approach.

Furthermore, a related issue to collateral mentioned above is talking about whether secured loans are riskier than unsecured loans. On the one hand, collateral decreases the riskiness of a given loan since it gives the lender a specific claim against the borrower. If borrowers who pledge collateral are less risky than borrowers who do not, then secured

loans are necessarily safer than unsecured loans. In contrast, if borrowers who pledge collateral are more risky than borrowers who do not, then secured loans could be either safer or riskier on average than unsecured loans.

The theoretical dispute, between the collateral and the borrower's credit risk, has been scrutinized by [Allen B. Berger and Gregory F. Udell, 1988] **(9)** who came to the conclusion that “among types of related risk: the riskiness of the borrower; the riskiness of the loan; and the risk of the bank,...there is a positive relationship between collateral and risk.. Riskier than average firms tend to borrow on a secured basis; the average secured loan tend to be riskier than the average unsecured loan; and banks which make a higher fraction tend to have riskier loan portfolio.”

The implication of such results from the bank's point of view is based on that a bank with a higher percentage of secured commercial and industrial loans would apply a penalty on secured lending, which would reduce a bank's risk. Such a penalty, however, could also increase risk in a way that people would not be encouraged to borrow on the basis of secured loans.

The above discussion shows that the assessment of loan risk carried out by banks is not an easy task and it is one of the most contentious areas within the scope of the bank's credit decisions. Solving such matters, partially, the securitisation procedures can enable banks avoiding risks that may appear in the case of loans.

III-Asset Backed Securitisation (ABS) approach

III-1 Understanding securitisation issue

III-1-1 Definitions

Securitisation definition can be viewed from three different angles: accounting, economic, and banking.

From the accounting point of view, securitisation is seen as “an arrangement involving on party (the Originator) selling a portfolio of high quality assets, such as houses mortgages, to Special Purpose Vehicle (SPV) (the issuer), who issues loan notes to finance the purchase. The arrangement is a form of off-balance sheet finance”. **(10)** Economically speaking, securitisation is “the packaging of numbers of non-marketable assets, such as mortgage loans, into bundles which are marketable. Individual mortgages are not normally marketable because there is too much idiosyncratic risk in dealing with any one of them. A package of several similar mortgages reduces the riskiness, which allows the package to be marketed at lower interest rates”. **(11)** As far as banking activities are concerned, securitisation can be defined as “a process that enables borrowing and lending by banks to be replaced by the issue of such securities as Eurobonds. If a borrower can borrow directly from an investor, by issuing them with a bond (or equity), the cost to both borrower and lender can be reduced”. **(12)**

To sum up, it can be said that securitisation is the conversion of cash flows originating from a single asset or group of assets into financial instruments such as commercial paper or floating rate notes which are then sold to investors. Securitisation differs from factoring in that the relationship between the corporation and debtor is maintained. **(13)** So, securitisation means that if the asset flows it can be securitised. That means again, if any receivable generates cash flow it can be considered for structured financing.

III-1-2 Securitisation process

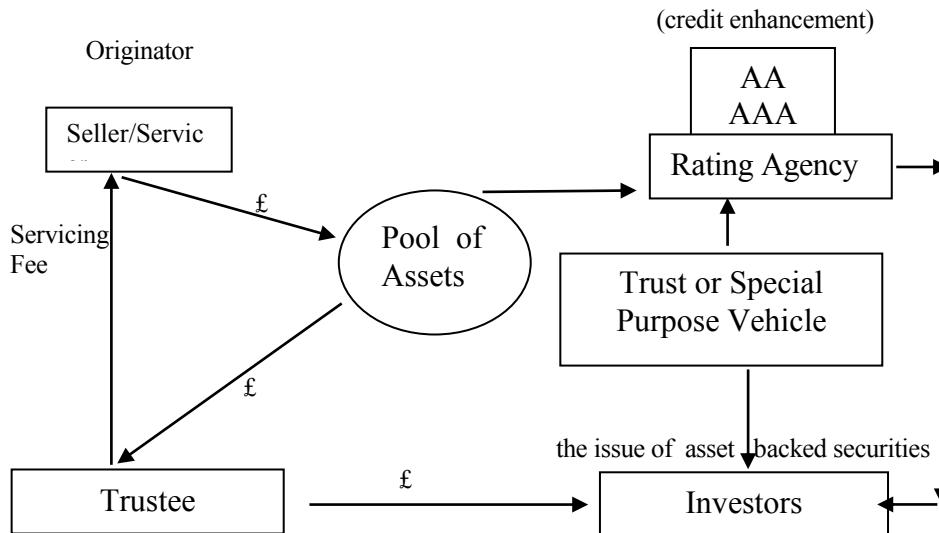
Generally speaking, Securitisation process is broken down into five parts: origination, structuring, credit enhancement, trading, and servicing.

Securitisation starts when a company originates and puts together a pool of underlying primary assets which can be sold as specific receivables. Typically, the originator (the seller or the servicer), as is shown in the diagram below, sells a pool or a bundle of assets to a Special Purpose Vehicle (SPV) that is set up for the purpose of structuring the transaction. Then, the (SPV) determines the tax and accounting structure of the transaction as well as structuring the relevant operational details, such as the payment structure of the notes and the protection against bankruptcy risk.

Sometimes, obtaining an investment-grade credit rating and making the transaction attractive to investors, it is necessary to have a credit enhancement procedure. The role of (SPV) is specified for guarantying a partial amount of potential losses of assets that are securitised. This procedure is similar to the reinsurance contract in the property casualty business.

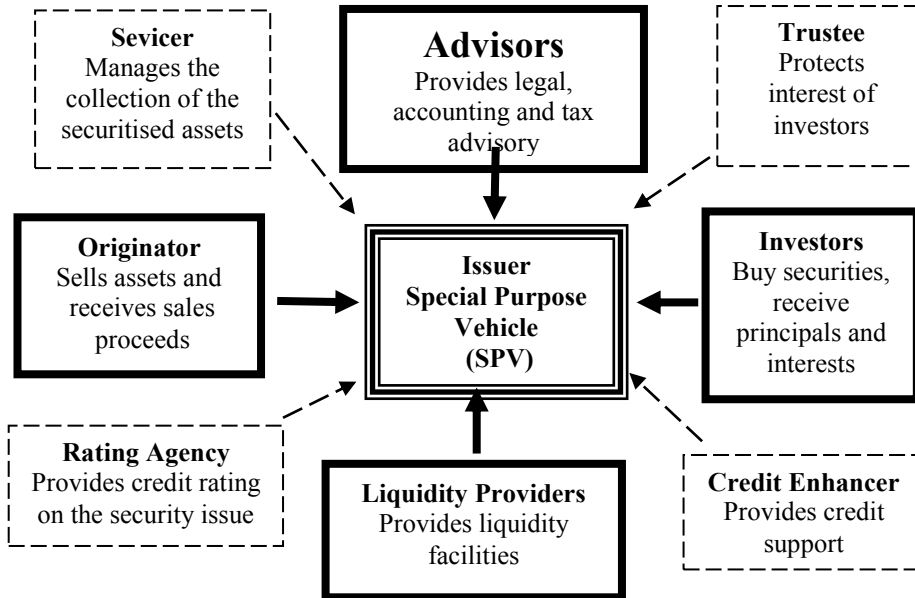
Furthermore, the placement and the trading of assets are achieved through the (SPV), and are usually in the form of very high rated issue of notes that are frequently bought by institutional investors, or mutual funds. The underlying assets can be serviced either by a third party or by the originator who has retained the spread (the difference) between the yield on the assets and the interest paid to investors, not of credit enhancement and other fees. The spread account is deposited into an account that is available to cover delinquencies and losses of the loan. (14) Thus, the following figure shows the basic structure of an ABS.

Basic Structure of an ABS



£: it means receivables cash flow
 Source: Smallman and Selby (15)

As it is explained above about the mechanism of securitisation process based on the above figure proposed, it would be better off providing details concerning the relationship of the issuer (SPV) with all principal and subordinated parties that are important for the function of securitisation process. Therefore, the following figure is as an example:



Source: Charles Loh, (16)
 <<http://www.spring.gov.sg/portal/attach/A3%20-%20Mr%20Charles%20Loh-2004-2-191857.pdf>>

III-1-3 Securitisation Characteristics (17)

Securitisation as means of modern financing is characterised through four elements as follows:

- First, the credit risks of the original lender are isolated from the transaction through the use of a separate legal entity or SPV which holds the receivables and issues the securities. In this way, the security often enjoys a higher credit rating than the original loan receivables ;
- Second, through the pooling of a diversification portfolio of receivables, unique risks in each loan are reduced for the investor ;
- Third, securitisation allows the risk in the receivables to be allocated to different parties.
- Finally, cash flows may be repackaged and tailored to specific investor preferences or opportunities in the yield curve, where a reduced cost of funding can be achieved.

III-2 Securitisation benefits

Securitisation offers the benefit of lowering the costs of funds by isolating the risk. With the asset backed securities (ABS), investors buy a specific set of receivables with a known amount of risk. This is far safer than dealing with investors, who in turn, at their discretion, fund existing assets or purchase riskier ones. The uncertainty of the assets' risk degree obliges banks to demand higher rates of interest which makes it more costly than the asset backed securities.

Benefits from the use of the asset backed securitisation method can be confined in that first, it allows companies with low credit rating to borrow funds at AAA rates. Also, in most cases the cost of constructing ABS is less than the cost of equity to support the debt issue. Therefore, the freeing of capital and the lower intermediation cost can be considered as the two important economic benefits that stimulate the market growth of the ABS. In addition, there are other advantages which can be expressed in terms of fee income, off-balance sheet financing, and risk management.

III.2-1 Free income

"Securitisation offers a mechanism for an institution to grow its sources of fee income without straining the balance sheet. As a result, a bank may achieve a higher return on equity capital and a higher quality of return, as interpreted by those banks analysts who favour predictable sources of non-interest income rather than highly volatile earnings pegged to interest rate fluctuations" [Kopff and Lent, 1988] **(18)**. In other words, securitisation offers the prospect for originators to improve their return on assets by shrinking their asset base relative to the volume of loans originated while continuing to get the benefits of high volumes of loan origination. Such benefits include the ability to retain fee income in the form of servicing fee and potential for further gain through excess servicing and retention of residual interests in the cash flow generated by the securitised loans. **(19)**

III-2-2 Off-balance sheet financing

Since securitisation takes assets off the balance sheet, allowing banks with a tight capital structure to free capital, there should be a significant improvement in equity return. Therefore many more banks will look to securitisation to help manage their balance sheet costs. From the originator point of view the loans are not booked, where the interest rate risk will be more manageable.**(20)**

III-2-3 Risk management

Risk management can be broken into two main risks; interest rate risk and credit risk. The former means that companies transfer the interest rate to the holder of an ABS, which can be extremely advantageous to finance companies that are highly sensitive to interest rate fluctuations. While the latter explains that risky assets can be transferred in a way that an off balance sheet helps a company's credit standing. In other words, credit risks of the original lender (originator) are isolated from the transaction through the use of Special Purpose Vehicle (SPV) or a trustee which holds the receivables and issues securities. In this sense, the securities often enjoy a higher credit rating than the original loan receivables, which can be achieved by the intermediation of the bank or any other financial institution.

Moreover, Securitisation allows receivables that incur risks to be allocated to different parties which can be a third party or holders of subordinated securities. (21)

Thus, it can be said that the management of interest rate risk, on the behalf of a finance company or a bank, is another impetus for securitisation. Fixed- rate assets that are funded with variable rate deposits may be securitised to reduce interest rate risk. In United States, Belgium, and France where home mortgage interest rates are often fixed, the reduction of this kind of risks can constitute an important motivation for securitisation. However, in the United Kingdom, Australia, and Canada where the mortgage lending is customarily done on a variable rate basis, securitisation appears to be less attractive since the motivation of reducing the interest rate risk of this particular kind of assets is missed.

Risk analysis can be achieved through the rating process. This starts when the issuer approaches the agencies before it registers the ABS with the Securities and Exchange Commission to discuss the rating parameters. The issuer, or its investment banker, meets the cash agency to discuss the structure of its transaction and to introduce the agency to the nature the issuer's business and its operations. Therefore a delinquent receivable can be traced through the system of rating process, where the agency will make the recommendations on procedures to segregate the pooled receivable for tracking and reporting purposes.

However, securitisation cannot be treated as a perfect mean of financing without certain deficiencies. The major drawbacks that are put forward against investing in ABS are concentrating on the inherent risks that the investor may face when the securitisation process is taking place.

III-3 Risks from Investing in ABS

As well as the listed advantages already mentioned above, concerning the asset-backed securities as a new source financing, the risks of securitisation for the investors have already been stated. For instance, [William A. Hayes, 1990] (22) illustrated that the inherent risks in the securitisation process can be summarised in the following points: fraud, erroneous legal and representations, poor performance credit downgrades, prepayment, and concentration.

III-3-1 Fraud

Fraudulent activities could involve any of the participants in the securitisation process- originator, servicer, trustee, accountants, lawyers, or investment bankers- and may occur in any aspect of the financing arrangements. Although some procedures or a diligent investigation can be conducted to protect the investor from the fraud, it has been experienced that fraud risk can occur. Recently in the United States, the Guardian bank in New York was closed by the highest authorities as a result of an alledged fraud in its mortgage-backed securities program.

III-3-2 Erroneous legal and representation

The application of securitisation is more developed in the United States than in other places in the world then, it is clear that the risks of securitisation can be easily identified under the American regime. In terms of the legal risks, the law would not be able to account for all the representations of opinions and therefore there should be areas which are subject to ongoing uncertainties and potential change. This includes the interpretations of federal and state laws and regulations, the sales and pledge status of underlying assets,

failure of the trustee to perfect a security interest in the underlying assets, and unattached cash flows of the underlying assets. As part of the protection against any legal risks, an institution's legal counsel (Advisors) should review all agreement, contracts, and legal opinions before the banks accept asset-backed securities for investment portfolios. In this sense, risks can be identified and the transactions can fully comply with the regulatory requirements.

Yet, representation risks can arise by two important means. First, when investors rely too heavily on investment bankers, appraisers, and others to provide opinions that are used to establish a credit rating for an asset backed security. Second, prior to completing the securitisation process, the issuer has the ability to substitute the collateral that may not be similar in type or quality to the original collateral described in the issue's prospectus.

III-3-3 Poor performance and credit rating downgrades

Credit rating downgrades is another risk that may have an impact on asset-backed securities investment. This has been proved through many more evidences. For instance, it has been reported that U.S. \$6.5 billion of structured financing was downgraded during 1988; meanwhile an additional \$10 billion of structured financing was revised for potential rating changes. Such downgrades can affect the marketability of a security issue and consequently lead to liquidity problems for an institution that has a concentration of these securities in its investment portfolio.

Furthermore, performance risk results from the possibility that third party participants in the securitisation process (i.e., servicers, or trustees) will fail to fulfil their contractual responsibilities. Another example related to this type of risks is the inadequate or the protection provided through credit enhancements, such as collateralisation, insurance coverage, or letter of credit. Therefore, the investment officers should ensure that the financial condition of all parties involved in the process is strong, that credits enhancements are adequately protected against potential losses.

III-3-4 Prepayment

The primary consideration for prepayment risk is related to securities formed from stripped security issues. Stripped security means the security that may take the form of interest-only (IO) or principal-only (PO), which can be sold at a discount similar to zero coupon bonds. And the investor receives either all the interest cash flows or all the principal cash flows from the underlying collateral. Therefore, any increase in interest rates could increase prepayment of the loans in the underlying collateral pool, thereby increasing the value of PO strips, because the prepaid principal has a higher present value than that of future payments would have. However, increased prepayment would decrease the value of IO strips since the future interest income earned on the underlying principal is reduced in proportion to the prepaid principal. Thus, prepayment presents a potential loss to the IO strip investor if it becomes necessary to liquidate the security. (23)

III-3-5 Concentration

In addition to all risks mentioned above, it can also be said that the relationship between the participants, including investors, is an important risky factor as far as the implementation of the securitisation process is concerned. Any concentration of investments in one particular issue or in a particular type of issue (like automobile loans, or credit cards receivables that are extremely sensitive to economic conditions) creates investor risk. Therefore, close interaction of participants and the investors could create

systemic liquidity problems. Such problems could occur when one or more of the participants fail to fulfil their obligations.

IV- The ABS' challenges to the bank's role

IV-1 Macro and micro-economic approaches

It has been observed that the intense competition from nonbanks that has led to the innovation of ABS has critically affected the banks' role on both scales domestically and internationally. For instance, in the United States, and during the decade of 1974-1984, commercial papers growth used by the intermediation of banks exceeded commercial and industrial loan growth (16.5% and 8.5% respectively) (24). However, the bank profits have declined during the period of 1980 and 1985 that matches the growing increase of ABS. In this sense, it can be said that ABS presented itself as a new alternative in the market so as to face the problems that banks, to some extent, were unable to solve.

On a macroeconomic approach, factors that were the cause of the banks' profits decline are higher than inflation, fluctuate interest rate, and cyclicity of loan provisions. Alternatively, structural changes such as the decline of wholesale lending, deposit interest rates, deregulation, and a secular uptrend in loan loss provisions were the dominant contributors to the erosion of banks trends.

Based on a micro economic approach, banks thought that commercial and industrial (C&I) loans can possibly be securitised, as a result this may well assist in the rapid spread of securitisation use. Regardless of the benefits of (C&I) loans securitisation, which are similar to other types of securitised assets, the barriers that stand in front of this kind of assets are much more difficult.

The major practical obstacles, related to the securitisation of (C&I), are those concerned with tax and legislation. (25) To overcome such barriers relaxed and flexible rules from governmental and financial institution authorities are very appreciative. In this context, banks interested in securitising (C&I) loans should consult with their advisors on these important issues.

Other obstacles from securitising (C&I) loans, that are suffering the marketability and the successful spread in the market, are as a result of two reasons: first, it can referred to the engagement of rating agencies in examining loans, and second, for the possibility of banks, in case of developing the level of over collateralisation that might mitigate the need for close consideration of the credit's characteristics of the underlying loans.

Unlike commercial and industrial loans, other types of securitised assets are characterised by certain degree of durational and predictability factors. These two factors are missing in the case of C&I loans which hinder the practical implementation of such types of assets. Investors need some degree of certainty as to when they will receive the return of their capital.

Moreover, the greatest engines driving the securitisation of mortgages and other consumer receivables is the ability of investment banks to earn profits by assembling pools of loans, operating conduit businesses and structuring and underwriting securities for the originators of such loans. In fact, C&I loans are lacking the adequate organisational structure needed for securitisation.

IV-2 The international scale

On an international scale there is more to say about the real challenge of ABS to the traditional financing function of banks. The existence of securitisation since the beginning of the 1980s has obliged international bankers to change their policies to the point that a simple spread account rule 5:6:5pm needs to be changed to 8:8.1:8pm. This means, for the former, that banks were taking deposits at 5 per cent, made loans at 6 per cent and closed at 5 pm. The same argument can be developed for the latter under the new rule.

Furthermore, it has been evidenced that the share of international financing, from the period 1981 to 1986, in the form of securitisation increased from 33 per cent to 85 per cent. Further than that, the period of the mid 1970s until 1987, prime borrowers in the Eurocurrency markets paid as much as 1 1/4 per cent at the beginning of the period whereas only less than 1/8 per cent of the spread has been paid at the end of the period. Again, this evidence shows on one side fierce international competition and on the other the deference of the banks' role in the world of financing.

During the 1970s, the importance of banks in international credit intermediation appeared to be well established until the beginning of the 1980s, especially when the debt crisis erupted in 1982. This view has been supported by several studies like [John M. Atkins, 1987] (26), [David M.W. Harvey, 1991](27) who ascertained that the birth of securitisation, in addition to that period of crisis, was a result of the inability to manage so many problems at the level of banking activities, some of which have already been mentioned.

Other evidence of equal importance asserted that the ratio of bonds to credit finance supported by banks, which was around 1:5 at the beginning of 1980, has been reversed to 2:1 in the year 1985. Meanwhile, the syndicated eurobank loans decreased from 68 per cent to 9 per cent within the same period. Thus this trend clearly shows that the capital intermediation market has been replacing the 1970s domination of banks within the international credit intermediation scale.

IV-3 Market school vs. Banking school

Securitisation has stimulated the appearance of two opposing schools. [Gardener, 1987] (28). The first one is called the "market school" which believes that securitisation implies the inevitable decline of the international banks' role. Further, the more extreme opinion from this school suggests that securitisation could mean the end of many kinds of bank functions altogether. This view can be logically accepted because it can be argued that as the number of the securitised transactions continue to grow, the technology will start to break up the functional roles of banks. With this desegregation, banks will concentrate their efforts on some of the following functions depending on where their strengths lie: originating, assembling, structuring, distributing or servicing transactions. Consequently, they will be disintermediated away into a much reduced role in financing activities and general resource allocation within society.

On the other hand, the "banking school" adopts a positive view concerning the role of banks which shows that securitisation is only another step in the modern development of the banking firm. Or, it could be a new vehicle to revive the traditional banking activities. Apparently, the banking school still has confidence in the innovatory and the adaptive powers of banks.

Consequently, banks have responded to these new challenges in three ways. Firstly, as was mentioned above, spread accounts have been reduced to the lowest levels in order to compete directly with the debt market rates. However, the shrunk of lending spread, on a

risk adjusted basis, provides reasonable returns. Secondly, as previously cited about the relationship between the credit risks and borrowing, banks started to focus on a strategy of higher risk borrower and meanwhile repricing the loans to offset for the greater risk. This affects the loan portfolio's quality so that the bank's risk profile can be increased. Finally, the strategy that could be employed to increase fee income from credit or non-credit related activities was not effective since it increases the risk profile. Different activities mean different risks associated with them.

Therefore, it seems that it is inevitable for banks to adopt the asset backed securitisation strategy. It has been argued [Kopff and Lent, 1988] (29) that for banks to adopt proper securitisation strategies, they need to make some changes, specifically, at the level of internal measurement such as corporate return on assets (ROA) and return on equity (ROE), fund transfer, capital allocation, and incentive systems. These changes are real challenges for the management to cope with in order to absorb the asset-backed securitisation.

V- Conclusion

It can be concluded that securitisation is a technique used to sell balance sheet assets to outside investors. It ensures compensation to investors with cash flows generated by the pool of assets sold. (30). Therefore, most financial and banking studies assess the role of securitisation which can be carried out for the future prospects, in a way that during the next few years banks themselves are more likely to increase their use of securitisation to respond to the new capital adequacy requirements. Nevertheless, developed countries economies as well as certain from other economies developing ones are going faster in implementing securitisation as a mean of effective financing.

Although most of those studies adopted in this study are pessimistic for the role of banks in the foreseeable future in coping with financing problems, the authors' opinions are still optimistic for the banking role in the financial market place. As a matter of fact, banking activities are being supported by governments in order to maintain their leading role in capital markets, especially money markets. Therefore, it can be said that there exists relative equilibrium between banks and the rest of capital market.

As far as securitisation and bank loans are concerned for being considered as means of alternative financing, it can be argued that the structure of banks is still well established and supported by central banks that are represented by the Basle Committee. However, banks are facing more challenges in order to cope with the enhancement of their capital ratios that is imposed by the same committee. Back in the mid-1970s, bankers were keen to boast about the size of their balance sheet, but now the only thing they want to publicise is their capacity to get rid of long term obligations, such as loans, and replacing them by more liquidate assets. In parallel, the shift from bank loans instrument to other alternatives started by concentrating on bonds and commercial papers.

Although bank loans are still not comparable with other financial institutions working in bond markets, it can be observed that the market infrastructure of the securitisation process is not strong enough to ease the application of the process. If barriers or risks from investing in securitisation, as already mentioned, cannot be overcome, then the asset-backed securities will no longer be attractive or beneficial.

Moreover, in the view of those who support the market capabilities in financial innovations, there were, however, some innovations which could not stay working efficiently for a long time in the market. For instance, the low grade or "Junk" bond market

that had known a dramatic growth in the beginning and the mid 1980s, later on suffered from a bad reputation in the market after the collapse of the Drexel Burnham Lambert, the Wall Street investment bank in the United States with the \$200 billion capital assets circulating over markets.

Nevertheless, the leading role of banks is still outstanding. For instance, the intermediation of savings through the banking system in the euro area is currently high in comparison with the USA (20%), though it ranges from over 80%, in Italy, and over 70% in Spain, France and Germany, to just over 50% in the Netherlands. (31)

However, it is expected that the disintermediation away from the banking system in Europe is more interesting for two reasons. On the side of banks' balance sheet, the expectation is to replace bank loans by bond issues, in response to the deeper and more liquid euro capital market. On the liability side, there is an expectation of shifting savings from bank deposits to bonds, equity, and investment funds, in response to demographic changes, pension reforms, and deregulation.

For the sustainability of banks in the market place, they should have an outlook beyond their own portfolio by giving securitisation service to other institutions including banks, thrifts, finance companies, and insurance companies.

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