

Public Procurement Contracts as an Effective Risk Management Strategy for Securitization

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Basics of securitization

Benefits of securitization

For borrowers:

- More favourable funding costs
- More stimulated lending environment

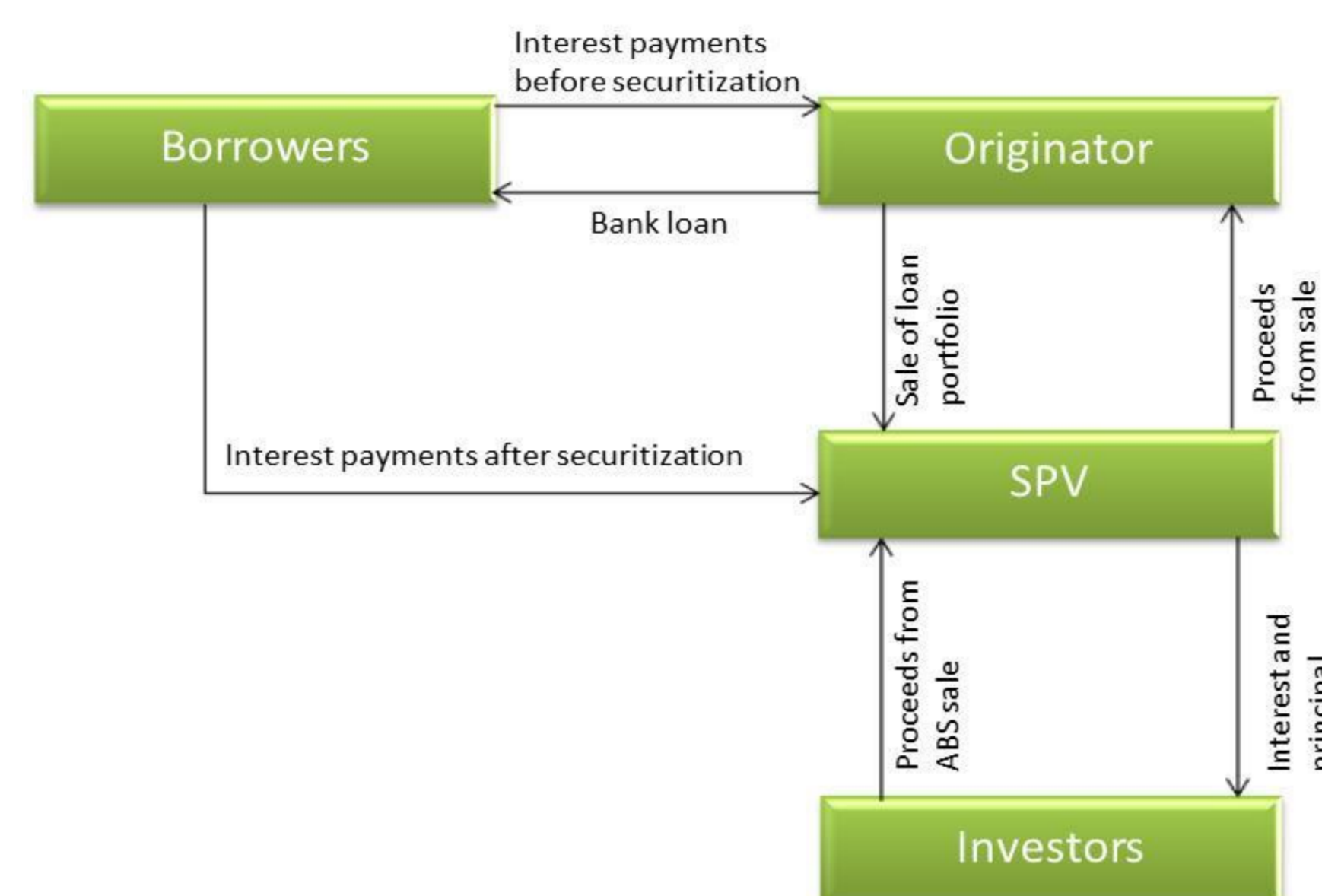
For banks:

- Capital release through freeing up balance sheet
- Secondary market for otherwise illiquid assets

For Investors:

- Exposure to hard-to-access sectors
- Portfolio diversification
- Attractive risk/return

Process of securitization



Criticism of securitization

- Limited transparency, opaque underlying structure
- Complex financial instruments
- Originate-to-distribute model – “cherry picking” of loans
- Synthetic securitization vs true-sale securitization
- Bad image due to involvement with US subprime crisis



Risks can be mitigated with appropriate structuring

Importance of SMEs

Definition: Small and medium sized enterprises (SMEs)

- < 250 employees
- < EUR 50 million annual turnover
- < EUR 43 million annual balance sheet

Role in the economy

- Essential for economic growth
- Employment: 2/3 of private sector jobs (around 75 million jobs) and represent 99% of all enterprises in the EU
- Major source of innovation and entrepreneurial skills
- Frequently use local technologies and skills
- Tendency to curb monopolies and develop service industry

Securitization for sustainable growth

Current situation:

- Sufficient capital is bloodline of every economy
- SMEs face serious difficulties with access to finance
- Bank deleveraging – banks quick to cut lending to SMEs
- Lending to private sector has been decreasing since the crisis (ECB)

Solution:

- Securitization is a fundamental tool to encourage banks to increase their lending appetite
- European SME securitizations market remains limited, unfavourable risk/return for investors – public intervention needed!

Example

First SME loan securitization in China

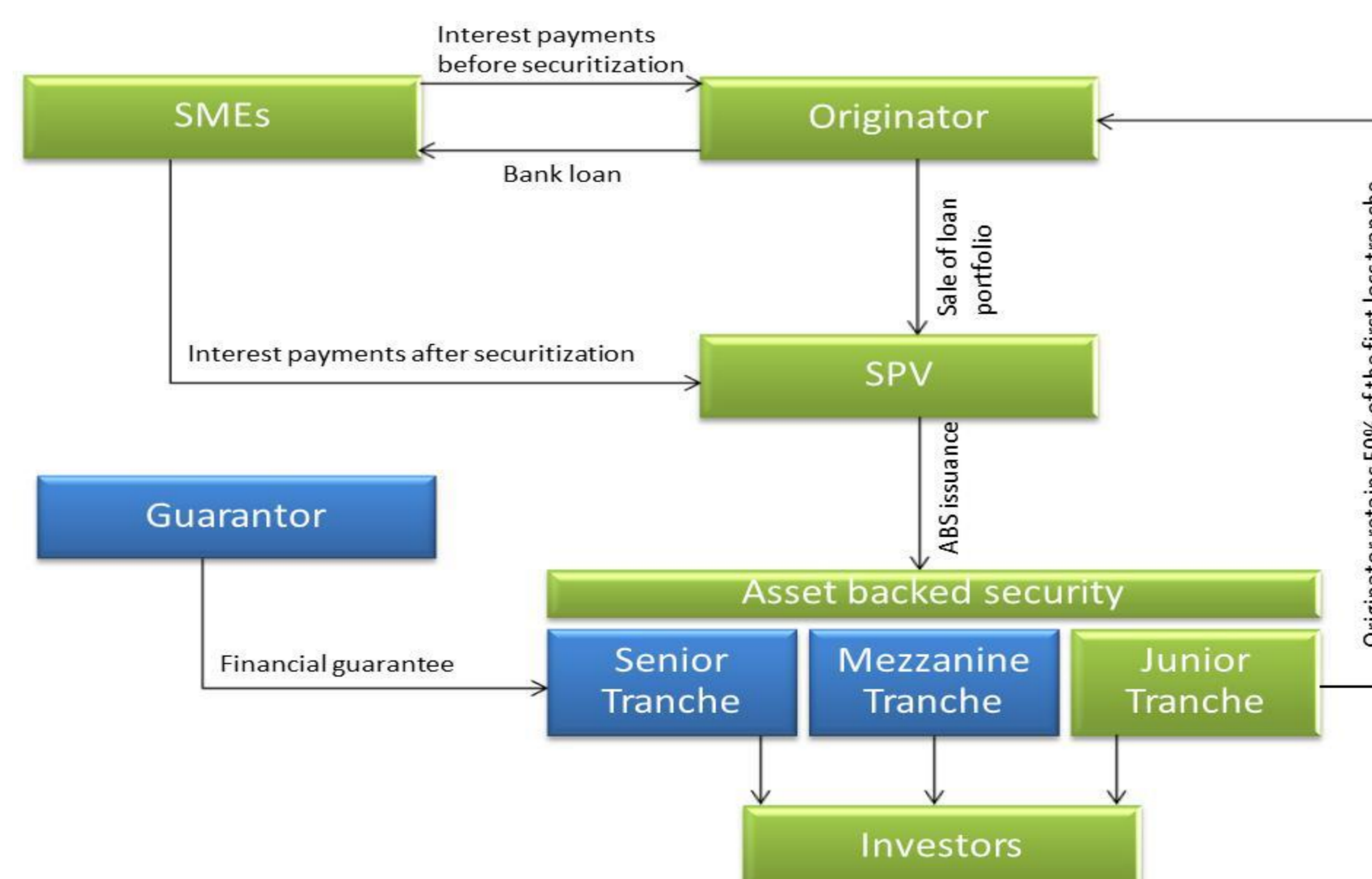
- Alibaba Group issued CNY500 million ABS backed by SME loans
- Post-deal situation: loans to 300,000 SMEs
- After deal situation: 500,000 additional loans to SMEs
- First out of the ten issues planned by the company

Credit guarantee schemes

Banks rate guarantees as the most effective government intervention to ease SME financing (World Bank)

- European Investment Fund guarantee facilities:** Guarantees for SME loans, securitized SME financing instruments; additional EUR 8.6 billion lending to SMEs in 2013
- Technology Fund in Switzerland:** Loan guarantees for Swiss companies with innovative technologies in greenhouse gas emission reduction, promotion of renewable energy sources and conservation of natural resources

Public procurement contracts as a risk management strategy



- Loans of SME businesses taken to fulfil green public procurement contracts would be eligible for the guarantee
- Scheme stimulates lending to SMEs and encourages their participation in green procurement bids

Accommodating regulatory environment is essential for ABS!