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# Report From ABS East 2011

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# Report From ABS East 2011

***(Editor's Note: This summarizes a number of speeches and panel discussions at the ABS East 2011 conference held in Miami Beach, Florida, Oct. 16-18, 2011. These summaries are intended to reflect the views of the panelists, and are not intended reflect the views of Standard & Poor's Ratings Services.)***

The ABS East 2011 conference in Miami Beach, Fla., attracted around 3,000 attendees. The overall mood was subdued. Panelists emphasized many of the same issues that have challenged the securitization market for more than two years: home prices, foreclosures, loan modifications, conforming loan limits, the role of Fannie Mae and Freddie Mac, and regulatory uncertainty. In addition, several new issues received attention: European sovereign debt, European banks, the U.S. budget imbalance, U.S. political gridlock, and uncertainty about the U.S. economic outlook.

However, even with a subdued tone, the mood of the conference may have been more positive than conditions warrant. Perhaps the most chilling moment was during the heavily attended opening session on Monday. One of the panelists asked the investors in the audience to identify themselves by raising their hands. Several dozen did. So far, so good. The panelist then asked the investors to raise their hands again if they planned to invest new money in securitizations. Only about six members of the audience raised their hands. The upshot: Until investors are willing to bring new money to the sector, the revival of structured finance will be stalled.

It is ironic that on the opening day of the conference, The Miami Herald's lead story was about the shadow inventory of distressed loans and foreclosure properties that will likely delay recovery of the housing sector (1). In true journalistic form, the story's introductory paragraphs described the core issue with unabashed directness:

"Officially, there are 3.5 million homes for sale nationwide. But there are millions more lurking in the shadows--hidden neatly away on banks' balance sheets, stalled in foreclosure court proceedings, or simply occupied by nonpaying owners as lenders wait months or years before taking action."

The housing market's ballooning shadow inventory--buoyed by a yearlong foreclosure slowdown--stands as its most menacing problem, threatening to stifle recovery for several years. Getting past the problems of previously overvalued residential real estate may be the critical step that must occur before nonagency securitization can bounce back. If that is correct, securitization professionals seemingly should want the U.S. real estate market to find its bottom as soon as possible, so that things can turn around and confidence can be restored. Interestingly, panelists at ABS East 2011 generally appeared to take an opposite view. They mostly advocated policies that would lengthen the period of dislocation in the housing sector in hopes of dampening the magnitude of the ultimate housing price decline. Even if such approaches represent good policy at a macroeconomic level, they seem contrary to the self-interest of the securitization industry. In other words, it would arguably be worse for the industry if home prices declined another 20% over four years than if they declined by 30% in one year before changing direction. In the former case, meaningful restoration of confidence might be five years away, while in the second, it could be just two.

Against the backdrop of significant challenges, there were several bright spots. First, although U.S. economic growth has been slow, the economy technically has been expanding since the third quarter of 2008. Second, although regulatory uncertainty continues to be an issue, the securitization industry is managing to adapt (albeit, sometimes grudgingly) to new regulatory requirements. Third, in the spirit of misery loves company (or maybe schadenfreude), compared with the U.S., Europe and China may be facing tougher challenges over the next decade in their real estate and financial sectors. Finally, and perhaps most important, despite the short-run challenges, the value of securitization as a financing tool in the U.S. is undeniable. The economic benefits of lowering the cost of funds; diversifying funding sources; and asset-liability matching virtually assure that securitization will have an enduring place in America's financial system.

The following summaries reflect the remarks of panelists at selected conference sessions. For the most part, they are based on the authors' notes, and have not been reviewed or approved by the panelists. We have tried to capture panelists' remarks accurately, and apologize in advance for any inaccuracies and omissions. In addition, we wish to acknowledge the excellent work of Information Management Network in organizing and hosting the conference.

## Sessions Covered

### Sunday, Oct. 16, 2011

- ABS Concepts and Terminology: Securitization 101
- Assessing Credit Risk in the RMBS Sector
- Bond Pricing and Valuation Tools
- Understanding the Role of Securitization in Revitalizing the Economy
- Keynote Address, Pimm Fox, Bloomberg

### Monday, Oct. 17, 2011

- Charting the Future of the Securitization Market: The Devil's in the Details
- Global Regulatory Initiatives and the Broader Impact on US Securitization Practices
- Keynote Address, James Lockhart, WL Ross & Co
- The Future of Mortgage Funding and the Impact of GSE Reform in the U.S.
- CLO 2.0: Market Lessons and Future
- Student loan ABS: FFELP and Private Loans, Recent Developments and Trends

### Tuesday, Oct. 18, 2011

- The U.S. Macroeconomic Outlook: Senior Economist Roundtable
- Piercing the Veil: Investors Speak Out on Transparency and Reporting
- Keynote Address, Joe Nocera, The New York Times
- Finding Relative Value in the ABS Markets: Research Analysts' Roundtable
- TRACE for the Structured Finance Market: Impact of Price Reporting on Trading Strategy
- RMBS Traders' and Researchers' Roundtable

## Sunday, Oct. 16, 2011

### ABS Concepts And Terminology: Securitization 101 (1:30pm)

***The participants:*** Securitization involves a large number of different kinds of participants to get a deal to market. Even before a deal's initial issuance, it requires bringing together roughly 10 different kinds of participants. The start of the process is origination of assets. Accounting rules must make sense. There must be a trustee for the SPE (special purpose entity).

The process of securitization used to work very smoothly before the financial crisis. However, for the past several years the flow of new deals has been very slow.



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***Credit enhancement:*** Credit enhancement is how credit risk is mitigated in a transaction. There are two ways to accomplish credit enhancement, internal and external. Internal credit enhancement comes from the assets included in a deal (e.g., overcollateralization or subordination). External credit enhancement comes from a third party, such as a guarantor.

***Fees:*** Some participants in a deal receive their entire fee at the deal's inception. These include bankers, lawyers, and accountants. Others receive their fees over the life a deal. These include servicers, trustees, and some others.

***Originate to distribute:*** This is a business model whereby a firm earns a profit by originating assets with the intent to sell or securitize them. Many firms operated successfully with that model in the early to mid-2000s, but the model broke down when the housing bubble burst and the financial crisis started. Before the originate-to-distribute business model became prevalent, many firms used securitization as one of several methods of funding. Under the originate-to-distribute model, securitization becomes the sole or primary method of funding asset originations.

***Popular asset classes for securitization:*** Popular asset classes for securitization include:

- MBS--mortgage-backed securities.
- GSE MBS--MBS issued or guaranteed by Ginnie Mae, Fannie Mae, or Freddie Mac.
- Private-label MBS (all other).
- CMBS--commercial mortgage-backed securities.
- ABS--asset-backed securities backed by auto loans, credit card receivables, student loans, and other mainstream types of receivables.
- CDOs--collateralized debt obligations; securities backed by corporate bonds, corporate loans, or by a combination of private-label MBS, ABS, and CMBS.
- Esoteric ABS--ABS backed by unusual or esoteric types of assets.

***Funding alternatives for originated assets:*** A lender or other originator of receivables has several alternatives for funding loans or receivables. Some methods involving selling the loans or receivables; some involve holding them as assets on the firm's balance sheet. The most common approaches are:

- issue common or preferred stock (equity);
- issue debt (corporate bonds);
- borrow from a bank (direct loan or line of credit);
- securitization; and
- "whole loan" sales.

Securitization can be an attractive type of funding because of its low cost. Achieving off-balance sheet accounting treatment is an additional factor that sometimes makes securitization attractive. However, changes in U.S. accounting rules over the past several years have made it more difficult to achieve off-balance sheet treatment for securitizations (FAS 166).

***Range of securitization products:*** Different types of securitization investments give investors different ways to "gain exposure" to different asset classes along with different combinations of risks and rewards. For example, an investor can gain exposure to the mortgage sector through either MBS or CDOs backed by MBS. However, the two types of investments might offer different combinations of risks and opportunities.

***Structure of securitization:*** The structure of a securitization can be complex. It can include both a "primary servicer" and a "master servicer." The primary servicer handles direct contact with the obligors/borrowers on the underlying receivables. The master servicer oversees the activities of the primary servicer(s) and aggregates the collections from multiple primary servicers. Some deals include a "special servicer," to handle loans that become seriously delinquent. A special servicer has expertise in collecting delinquent loans.

***Documentation for a securitization:*** A prospectus is an offering document for the sale of securities, and includes the disclosures required under securities laws. A securitization deal almost always has a main governing document--a contract--defining the terms of the issued securities and the rights and responsibilities of the parties, including the responsibilities of primary and special servicers. This often is called a "pooling and servicing agreement." Sometimes a deal's governing document is called an "indenture," in which case there is usually a separate "servicing agreement."

***Trustee:*** The trustee of a securitization has various administrative responsibilities; if the issued securities default, the trustee's duties expand. If a default occurs, the trustee has fiduciary responsibilities and is supposed to serve as the champion of investors' interests.

***Representations and warranties:*** SEC Rule 17g-7 requires rating agencies to report on the representations and warranties in a securitization deal. SEC Rule 15Ga-1 requires an ABS issuer to report on repurchases of assets for breaches of representations and warranties in its past securitization transactions (2).

### Assessing Credit Risk In The RMBS Sector (2:20pm)

***Collateral trends:*** The nonagency MBS sector has $1.2 trillion outstanding; 70% of the total is performing loans, and 30% is nonperforming loans. About 30% of the performing portion are "reperforming" loans, or those that have been modified. About 65% of delinquencies are subprime loans; about 30% are so-called "alternative-A" loans.

One panelist says there is a strong correlation between loans that are delinquent by 60 days or more and the "sustainable value ratios" of the underlying homes (i.e., the ratio of the "sustainable home price to the amount of the related mortgage loan"). The panelist estimates continuing erosion of borrowers' equity in their homes will offset the effect of any improvement in the unemployment rate on default risk. Loan modifications display limited effectiveness because the monthly payments on the modified loans are still not sufficiently affordable for borrowers. The recidivism rate on modified loans is very high for two reasons: The modified loans still take too much of borrowers' income; and modified loans still leave borrowers with underwater loans (i.e., a loan that exceeds the value of the related home). Even with principal reductions of 20%, modified loans still experience a re-default rate of 40% within two years.

On average, defaulting borrowers can stay in their homes for 33 months without making payments in a judicial foreclosure state. In a nonjudicial foreclosure state, the time is 26 months.

A loan modification involving re-underwriting the borrower's ability to afford the modified payments is more likely to succeed than one that ignores the affordability issue. One panelist says there is an emerging convergence of the success rate of modifications under the government's Home Affordable Modification Program (HAMP) loan modification program and those done under lenders' proprietary modification programs. However, data from the Office of Thrift Supervision suggest that modifications under lenders' proprietary programs and modifications of loans not included in securitizations are continuing to be more successful than modifications under the HAMP program.

One panelist expresses strong reservations about the "moral hazard" associated with modifications that reduce a loan's principal balance. The panelist notes that normal human behavior, self-interest, and psychology indicate that a borrower will act strategically in deciding whether to default and how to exploit loan modification programs.

***Credit analysis and ratings:*** One panelist argues that investors would be best served by models that offer output in the form of continuous numerical scores (e.g., 1-100), rather than the letter rating scales from credit rating agencies. In addition, an investor that purchased (or written down) a security to a deeply discounted value from par is better served by a credit risk analysis that focuses on the projected recovery on the security. This means that standard rating analysis, which might not differentiate two defaulted securities based on their recovery prospects, is less useful than an analysis that focuses on the recoveries.

***Representations and warranties:*** One rating agency equates the recent crisis with a single-A level of stress. It intends to call for extra credit enhancement in securitization deals based on the asset originators' financial capacity to perform on their representations and warranties (i.e., to repurchase assets that breach representations or warranties). Another panelist says there is no amount of credit enhancement that can make up for poor due diligence on the quality of mortgage loans included in a securitization. The panelist says the uncertainty associated with loans that materially breach representations and warranties is simply so great that no amount of credit enhancement can properly address it.

***Servicer impact:*** One panelist argues that investors should avoid deals that have high "stop advance rates" (i.e., a high proportion of delinquent loans on which the servicer has stopped advancing) and deals with a high proportion of loan modifications. These categories essentially are deals that have aggressive servicers. There is a wide divergence of behavior among servicers. Trustee reports give too little information on loan modifications. It is possible to analyze the impact of various servicing behaviors on the different securities in a deal.

## Bond Pricing And Valuation Tools (3:25pm)

One panelist says the best program or database is one that end users make for themselves. However, that is not practical for most structured finance investors because gathering data is so laborious and the cash-flow modeling so complex. A user of valuation products must be able to understand exactly how valuations are produced. Therefore, it is incumbent on the providers of valuation services to be transparent about how they produce valuations. However, even with transparency, different valuation providers apply different approaches that may produce conflicting valuations, especially for illiquid assets. For mortgages, questions that a user of valuation services should consider include:

- Does the valuation company use correct loan level data?
- Does the valuation company model the liability side of the subject transaction correctly?
- Does the valuation company focus on the appropriate scenarios for estimating values?
- Does the valuation company show all the steps of its analysis in reaching its conclusions?

Another panelist says a key issue for an investor should be how a valuation company captures market volatility in its valuations. The panelist says "fair market value" is the objective of valuation, and it must be distinguished from fast liquidation value. Another panelist notes that valuation companies face tough challenges because less than 1% of the fixed income market trades on any given day. Defining cohorts (e.g., by product type, vintage, and amount of credit support) for valuation benchmarking is challenging but extremely important. The cohorts allow investors to assess the reasonableness of valuations on specific securities.

Credit ratings play less of a role in valuations today than they did several years ago. One panelist says credit ratings have too little transparency for effective use in valuation.

Providing transparency is a key way a valuation company helps investors challenge a valuation. Investors may challenge a valuation from a valuation company if they have a materially different view of the most appropriate scenario (prepayment and loss vectors) for pricing the subject security. One vendor emphasized the need to consider the sensitivity of the implied fair value to small changes in scenario parameters. In other words, the vendor's approach looks for valuation "cliffs" across the range of scenarios.

One vendor is about to offer a system that will show a user how every dollar from a deal's underlying receivables gets allocated through the mechanics of the deal's cash-flow allocation waterfall.

One panelist emphasizes that valuation companies are most likely to produce differing valuations on "cuspy" bonds (i.e., those with valuations that are the most sensitive to small changes in the rates of prepayments and losses). Another panelist says a valuation process uses the pricing on actual trades as much as possible to compare with modeled/analytic valuations. An investor should use pricing on actual trades to test the reasonableness of valuations it receives from a valuation company.

One panelist expresses frustration at trying to reconcile small or moderate discrepancies in actual prepayment cash flows compared with the prepayment speeds used for pricing and valuation. Another panelist says the low level of cash flow detail available for agency deals (i.e., MBS from Ginnie Mae, Fannie Mae, or Freddie Mac, and student loan ABS from Sallie Mae) relative to private-label deals.

One panelist returns to the two basic challenges of pricing and valuation tools: projecting the cash flows on the underlying receivables; and modeling the cash flow allocations (waterfall) inside a transaction. The panelist notes that unanticipated, one-time events, such as litigation settlements, can have sudden effects on valuation. However, the effects of litigation settlements can be highly uncertain until the allocation of settlement proceeds to individual securities is complete. A significant portion of the trading community does not want to include such cash flows in bond valuations.

### Understanding The Role Of Securitization In Revitalizing The Economy (4:15pm)

The funding needs of the private sector will not fit onto the balance sheets of the world's banks. Thus, capital markets must supply some other way of funding assets that had been funded with securitization before the crisis. Many of those assets will continue to be funded with securitization. (Note: The funding capacity of the world's banks implicitly reflects banks' current levels of capitalization and leverage.)

One panelist says securitization will be necessary for the revival of the economy. However, certain types of changes are necessary--policy changes, changes in roles, and changes in infrastructure.

***Policy:*** On the policy side, the market is looking for standardization. Consistent data standards would make it easier for investors to figure out what they are actually holding. The creation of a centralized tracking number for each loan would make it easier (and practical) for tracking a loan through its entire life. There should also be verification of a loan's attributes to provide a "stamp of approval" that could travel with a loan through its life. The idea is to provide greater detail and reliability in the data available to investors.

***Roles:*** One kind of new role would be a quality reviewer to check the quality of loans. A second would be an investor representative to champion the interests of investors when there are disputes about whether other transaction parties have fulfilled their obligations. A third would be a data agent to help investors with compliance, risk management, and investment decisions.

***Infrastructure:*** One panelist argues that the mortgage industry should convert to a paperless business model in which documentation for individual loans is entirely electronic. Imaging of paper documents is a potential intermediate step. Fully electronic mortgage documentation would make securitization transactions easier. It would be great if the mortgage industry could get away from moving around truckloads of documents. Another change the panelist suggested is a mechanism for centralized lien perfection. Such a mechanism might have other benefits as well, e.g., a central repository of mortgage information would help investors spot when a borrower claims to have five primary residences or primary residences in multiple states.

***Securitization increases credit availability:*** Securitization helped increase the availability of credit in the economy. However, it sometimes has had too little transparency, particularly when it involved repeated repackagings of the same receivable (e.g., a loan is packaged into MBS, which is packaged into CDO, which is packaged into CDO-squared). Part of the reduction in securitization activity relates to the larger issue of deleveraging of the financial system. Even with the contraction of securitization activity, there has been around $100 billion of ABS issuance activity so far in 2011. The asset-backed commercial paper (ABCP) market is smaller than it was before the crisis, but has not disappeared.

Companies are now more conservative in how they manage their balance sheets, and are not as quick to add incremental funding facilities as they were before the financial crisis. The contraction in securitization activity spans all asset classes. Securitization remains an important part of the funding structure of specialty finance companies.

***Regulation:*** One panelist says both the Federal Reserve Bank of New York and the European Central Bank have stated that securitization is an important source of funding. One panelist says 20% to 35% of economic activity in the U.S. is tied to financial services; therefore, recovery of financial services is necessary to recovery of the broader economy. On the other hand, there is a broad push toward simplicity, which is the opposite of the trend in securitization before the crisis. (The U.S. financial services sector, which includes banks, insurance companies, and securities firms, accounts for roughly 8% of GDP.) Europe has much more intrusive regulation than the U.S., and that is likely to remain true for the long term.

One panelist observes that the greatest impact of Dodd-Frank is on small business, and questioned whether Dodd-Frank aligns with the broader values of society. The panelist asserted that the real problem was mark-to-market accounting, and says the Latin American debt crisis of the early 1980s would have produced effects as great as those of the recent financial crisis if mark-to-market accounting had required banks to mark down their Latin American exposures.

### Keynote Address, Pimm Fox, Bloomberg (5:05pm)

***Deleveraging is the theme:*** The U.S. economy is sending mixed signals, some if which point to the possibility of another recession, while others point to a continuing recovery. There are two big proposals in Europe right now: One is an expanded European Financial Stability Facility, supposed to be leveraged from €400 billion to roughly €1 trillion. The other is recapitalization. Funding costs for European banks will likely remain high and the availability of funding will likely be volatile. The loss on Dexia is likely to be between €100 billion and €200 billion.

Bank assets in Europe are €25.5 trillion, about 235% of Europe's GDP. By contrast, bank assets in the U.S. are only about 75% of U.S. GDP. This suggests that recapitalizing European banks is a tougher task than recapitalizing U.S. banks. European banks are all likely to hold their impaired assets to maturity and then to cut lending all at the same time. The correlated behavior of the institutions may cause significant market disruptions. Bonds issued by the European banks make up half of the European bond market. Because banks hold most of the bonds, deleveraging is likely to cause a material widening of spreads. Liquidity in European bond markets will likely dry up.

There is a reasonable possibility that European banks will have to write down the value of their assets by 20%: That would be a hit of €5 trillion.

One way to accomplish deleveraging is through run-off. A second is through asset sales, but who would buy the assets being sold? European insurance companies would likely not be able to absorb a large portion of the banking sector's assets. The insurers have total assets of about €7 trillion, one-half of which is already in fixed income and loans. Likewise, the U.S. banking sector could not likely absorb a large share of assets from European banks. U.S. banks have $1.8 trillion in cash and another $1.6 in U.S. government bonds. A third method of deleveraging would be equity recapitalizations. One Italian bank is already trying this, but it is not clear whether it will work. Perhaps the European sovereigns will recapitalize the European banks. But that would essentially be a transfer from the center (France and Germany) to the periphery. A fourth method of deleveraging would be to increase deposits. About one-third of all European bank funding comes from deposits. Deposits at Irish and Greek banks are declining, and interest on deposits in Spain was very high over the summer because of a "war" to attract deposits. A fifth way to deleverage is consolidations.

And, if you think things are bad now, just wait for the Chinese real estate bubble to burst. China has built new cities that are virtually empty. One extreme example of the bubble is the South China Mall, built several years ago, but which is almost completely empty. China has 64 million empty apartments. The Chinese government continues the building to sustain economic growth, even though the production does not contribute to the betterment of anyone's life. The apartments are far too expensive for ordinary Chinese families to afford. Ironically, the urban housing for many Chinese is extremely crowded, with multiple households sharing small apartments. China has not experienced a U.S.-style credit explosion because credit terms are very onerous (high down payments and short-term loans).

## Monday, Oct. 17, 2011

### Charting The Future Of The Securitization Market: The Devil's In The Details (9:00am)

The audience included several dozen investors, but only a handful of them plan to put new money into securitizations over the next year.

***What is holding back growth of ABS issuance?*** One panelist says lack of loan growth is a reason for the slow revival of ABS issuance in many non-mortgage sectors. In addition, originators are using other funding strategies for their loan originations. A second panelist says ABS issuance volume cannot bounce back until the securitization industry repairs the ongoing problems that led it into the financial crisis. A third panelist highlighted the complete destruction of certain subsectors--bank securitizations, private-label MBS, and CDOs of ABS--and regulatory uncertainty as key factors holding back a revival of ABS issuance. Another panelist argued that general economic uncertainty (including the perceived risk of sovereign defaults) is a significant factor. Another highlighted the overhang of underwater assets and the economic environment (low growth and high unemployment). The panelist also says the high level of government involvement in securitization may be crowding out private-sector securitization activity.

One panelist notes that some investors have outsourced their securitization credit analysis to the rating agencies. Those investors may have decided to shift their focus away from securitization and toward markets that are simpler to analyze and which they can analyze in-house. Another panelist argues that securitization should not be viewed as a method of expanding the supply of credit (i.e., credit creation), but rather only as a method for funding receivables created in the ordinary course of normal commercial or financial activities. The panelist reiterated that the securitization industry should repair the problems that led it into the financial crisis. Another panelist says that although securitization is an important and viable means of financing, it may have already reached or surpassed its optimal size; it does not have keep expanding into new asset classes and structures.

An audience member says the securitization industry got too comfortable selling securities to the same narrow group of investors, and should embrace simpler products that can appeal to a broader base of investors, including pension funds. One panelist says structured finance securities currently are valued at a discount relative to their underlying assets, interprets the discount as an indication that securitization structures are adding uncertainty and complexity that drag down values.

***Risk retention:*** One panelist says risk retention proposals in the U.S. are too complicated (3). Europe embraced a simpler risk retention requirement (4). In the U.S., the Dodd-Frank law (§941) requires risk retention by securitizers. Another panelist says the risk retention provision should be repealed, noting that new regulations for improved due diligence and improved disclosure are positive developments and should eliminate the need for risk retention. A third panelist says securitization issuers will find ways to circumvent risk retention requirements. Overall, although panelists have differing views about the wisdom of a risk retention requirement, nearly all believe that it is here to stay.

***Rating agencies:*** One panelist says investors should not use credit ratings as the primary basis for making investment decisions; a second and third panelist agreed. One noted that the trend of removing ratings from U.S. regulations is a positive development (5), but the continuing use of ratings in Basel III is a problem (6). The panelist suggested that there should be a rule that restricts an investor to purchasing investments that it is able to analyze itself. Most panelists agreed that investors have placed too much emphasis on credit ratings. Another panelist says ratings are still critical to most investors for their compliance with Basel II and "Basel 2.5" (7). The impact of the Dodd-Frank imperative to remove ratings from regulation has not yet been accomplished.

One panelist asked if audience members would view greater expenditures on ratings as a good use of money. The issue is how to cover the expense of the additional analysis and other services that some market participants want from rating agencies.

***Outlook for 2012:*** One panelist says next year will have a reasonable level of issuance in most asset classes but not in private-label MBS; a second says the balance of power is back in investors' hands. The securitization industry must clean up the old mess before revival can happen. A third panelist believes 2012 will be slow, and plagued by both economic and regulatory uncertainty. A fourth panelist acknowledges the uncertainty, but notes there is a huge amount of capital looking for investment, and that smart investors will seize opportunities in securitization. A fifth says the securitization industry will likely be smaller, and that firms likely will become more specialized. A sixth panelist says policymakers should reduce the role of the GSEs by requiring them to stop under-pricing their guarantees. This could help support a revival of private-label MBS.

### Global Regulatory Initiatives And The Broader Impact On US Securitization Practices (10:00am)

Regulators were signed up to participate on the panel but they dropped out. One panelist says the regulators are too busy promulgating new regulations. The theme for the session is whether new regulations will help the securitization industry recover.

Based on discussions with regulators, one panelist expects a proposal for the U.S. implementation of Basel 2.5 should come in the fourth quarter of 2011 or the first quarter of 2012. Basel III likely will come in the first quarter of 2012. The panelist says there were so many issues with the original risk retention proposal that there will have to be a second proposal, meaning a final rule on risk retention is not likely for some time. The panelist has no prediction on the timing of a conflict of interest rule (8) or the implementation of the Volker rule (9).

***Risk Retention (10):*** One panelist says the underlying objective of risk-retention regulations is the same in the U.S. and Europe, but the methods are quite different. In the U.S., a securitizer will be required to retain risk; in Europe, risk retention requirements already are in effect. Final risk-retention rules for the U.S. are not yet in place. For

RMBS, there will be a one-year delay after publication in the Federal Register; for other asset classes, there will be a two-year delay.

Another panelist observed that the European version of risk retention is investor-focused, while the U.S. version is issuer-focused. The European version allows for unfunded risk retention. In contrast, the U.S. version will not allow unfunded risk retention. The U.S. version carves out certain assets, such as "qualified residential mortgages" or "QRMs" (11). Although the two regimes differ, global markets will have to deal with both.

A third panelist says the risk retention rules have many good features, noting that the exception for qualified assets--like QRMs--is a good feature, but in contrast believes the premium cash reserve account (12) feature is very bad. It essentially requires an issuer to hold a residual interest, and makes it impossible for securitizers to make a cash profit at the inception of a deal. The issuer would have to earn its profit over the life of a deal.

***Franken amendment (13):*** One panelist says the Franken amendment is a section of Dodd-Frank that calls for a study to determine the feasibility of creating a special board to select the rating agency or rating agencies to rate a securitization transaction. The purpose is to protect investors' interests by preventing rating shopping. Unless the result of the SEC study is a suitable alternative, the Franken amendment proposal is supposed to go into effect, which the panelist says would potentially increase costs. Additionally, it presumes that all rating agencies are equally competent. It also ignores the issue of investor preferences for certain rating agencies and removes investor choice (preference) from rating agency selection.

An alternative is to rely on Rule 17g-5 as the device to prevent rating shopping (Rule 17g-5 is supposed to make identical information available to all rating agencies so that they can do unsolicited ratings.) Regulators currently are not focused on the Franken amendment, because they are working on regulations that have an earlier deadline for implementation.

***Conflict of interest rule (14):*** One panelist says the conflict of interest rules are well designed and well drafted, in sharp contrast to the risk-retention rules. Under the conflict-of-interest rule, an issuer or arranger cannot engage in a transaction that would benefit from poor performance of a deal that it sold to investors for a period of one year after selling such deal. However, the rule contains exceptions for market making and hedging activities. The rule creates new oversight and coordination challenges for large financial institutions that might have different departments taking different sides of a trade. The panelist says the stringency of enforcement will be an issue if it prevents proper hedging and market making activities.

***Basel III:*** One panelist says the biggest issue with Basel III is the proposed "liquidity coverage ratio (15)." The idea of requiring banks to have more liquidity is good, but the regulation may go too far: It requires banks to hold unencumbered liquid assets to cover the 100% amount of net cash outflows over the next 30 days. The high coverage with liquid assets will increase the cost of lending broadly, and the cost of liquidity in particular. The financial industry is gathering data on the degree to which unfunded commitments were drawn down during the recent crisis, to argue to regulators that coverage of less than 100% should be sufficient.

Another feature of Basel III is the proposed "net stable funding ratio." This component of the liquidity proposal would essentially require financial institutions to fund liquid assets with short-term debt.

***Basel 2.5 (16):*** Basel 2.5 would essentially move assets from a bank's trading book to its banking book. Capital charges on banking book assets currently use ratings, but the thrust of Dodd-Frank is to stop using ratings to determine required capital. The order in which regulations come out will matter.

***Solvency II (17):*** One panelist says Solvency II is a capital regulation for European insurance companies. It is similar to Basel III, scheduled to go into effect next year. The regulation likely will motivate European insurers to favor investments with shorter tenors and higher credit quality.

***Volker rule (18):*** The Volker rule is a proposal to prohibit banks from engaging in proprietary trading or from sponsoring hedge funds: It is very long, and asks many questions. A key feature is whether a securitization transaction relies on either Rule 3c-1 or Rule 3c-7 under the Investment Company Act of 1940. The proposal would potentially restrict a bank's securitization activities. It might limit a bank's ability to sponsor asset-backed commercial paper programs, and might limit a bank's ability to make servicer advances in credit card securitization transactions.

One panelist says the European risk retention rule (19) dampened demand by European investors for CLOs, and likely will do so for CMBS. About $8 billion of CLOs were issued in 2011, and total issuance could reach $10 billion for the full year.

***Unintended consequences:*** One panelist says an unintended consequence of new regulation will be a lower volume of securitization and a lower level of credit; another says the high volume of new rules will cause a "freeze" of the market. A third noted that securitization has been an important lubricant to the availability of credit, but that the market must recognize that different sectors have displayed differing degrees of resilience; therefore, regulation should not be designed on a one-size-fits-all basis, but recognize performance differences. A fourth panelist says regulation should be crafted to promote economic recovery by releasing the $4 trillion of cash on the balance sheets of U.S. banks.

### Keynote Address, James Lockhart, WL Ross & Co (11:00am)

Both the financial sector broadly and the securitization sector in particular continue experiencing stormy conditions. Economic headwinds, including both conditions in the U.S. and the sovereign debt problems in Europe, make the situation tougher. The key issue is the mortgage market.

The aggregate amount of residential mortgage loans in the U.S. is about $13.5 trillion. (Note: The correct figure is roughly $10.4 trillion.) The GSEs (Ginnie Mae, Fannie Mae, Freddie Mac) account for 56% and banks hold 24%. The amount of commercial mortgage loans is about $4.5 trillion.

European banks rely much more heavily on wholesale funding than U.S. banks. For a sampling of U.S. banks, the average ratio of loans to deposits is 83%. For a sampling of European banks, the ratio is 145%, so European banks may experience pressure to shed assets. Residential mortgage securitization is dominated by the GSEs: They currently absorb about 95% of loan originations and the remaining 5% stays on bank balance sheets. Likewise, the GSEs dominate the multifamily sector, accounting for about 70% of total financing activity.

***Housing bubbles:*** Countries other than the U.S. have had housing bubbles: The bubble in Ireland was markedly worse than the U.S.' bubble; the U.K. has a bubble that has not yet burst. Recovery in the U.S. housing sector cannot really occur until the effects of the bubble work their way through the system. The overhang of foreclosures and underwater loans likely will be felt for several years. Residential mortgage loan delinquencies recently started to decline, but from extremely high levels. Cynics say delinquencies are declining because those loans are being modified or foreclosed (rather than curing the delinquency).

The delinquency rates in the residential mortgage loan portfolios of the GSEs are much lower than delinquency rates in the overall mortgage market. What killed Fannie Mae and Freddie Mac was not the quality of their mortgage loan portfolios, but that they had too much leverage and too little capital.

There are about 53 million outstanding residential mortgage loans in the U.S. Although 56% of the loans are with Fannie/Freddie (either in MBS or on Fannie's/Freddie's balance sheet), only 28% of the seriously delinquent loans are with Fannie/Freddie. Conversely, private-label securitizations have only 9% of all the loans, but 28% of the seriously delinquent ones. The FHA/VA programs have 16% of the delinquent loans, while banks and thrifts hold 20% of the delinquent loans.

***Preventing foreclosures:*** The government contracts for private-label MBS should be amended to authorize servicers to sell mortgages at a discount and to modify loans with principal reductions. The servicing strategy in a deal should be based on producing the best net present value for the trust. The GSEs should authorize short sales, and get more creative on managing and liquidating homes acquired through foreclosures (REO). Eight million borrowers are current on their mortgage loans, but those loans are underwater. There is a risk that those borrowers will "strategically" default (i.e., default even though they can afford to make their mortgage payments). HARP can modify the loans of such borrowers to reduce monthly payments and reduce or eliminate the motivation to default. A list of challenges for mortgage servicers:

- 4 million to 10 million foreclosures still to come;
- loan put backs (repurchases) and servicer advances;
- robo signing;
- state attorney general settlements;
- Federal consent agreement;
- GSE servicer standards;
- FHFA fee proposal;
- Lawsuits;
- MERS;
- CFPB examinations;
- Basel III;
- future of Fannie Mae and Freddie Mac;
- List of challenges for private-label MBS;
- securitization through Fannie Mae or Freddie Mac is cheaper;
- Dodd-Frank requirements;
- PLS (private-label securities) disaster and PPIP support;
- QRM - skin in the game;
- pooling and servicing agreements;
- rating agencies;
- ASF's project RESTART;
- servicers' standards; and
- future of Fannie Mae and Freddie Mac.

***Future of the GSEs:*** There are sharply divided views in Congress about what to do with the GSEs. The keynote speaker favors splitting each of the GSEs into a "newco" and an "oldco." The newcos would issue and insure MBS but would not receive government support. However, there should be a government backstop to protect against "catastrophic" losses.

Private sector companies also could create newcos. The goal is to return most of the secondary mortgage market to the private sector. Other key reforms would include strengthening the regulator and requiring mortgage insurers to have living wills. Also, America should rethink the 30-year, fixed rate, prepayable mortgage as the core mortgage loan product.

Risk retention will help the revival of the private-label MBS market. In addition, revival of the private-label MBS sector depends on a significant reduction of the conforming loan limit (currently $625,500).

Another idea would be a "deductible" on the insurance from newcos so that investors have skin in the game. Broad risk sharing among investors, originators, and issuers would be good thing.

The three most important things to get past the current problems in the mortgage sector are: recreating a viable private-label MBS by providing interim catastrophic insurance from the government; using HARP to refinance underwater loans at the GSEs; and allowing short sales to resolve defaulted loans in securitizations.

### The Future Of Mortgage Funding And The Impact Of GSE Reform In The U.S. (12:00pm)

One panelist expects the structure of the U.S. housing finance system basically to be unchanged in five years, mainly because change happens very slowly. Aggregate U.S. residential mortgage debt is $10.4 trillion. The value of all housing in the U.S. is about $16 trillion. Fannie Mae and Freddie Mac absorb about 63% to 64% of loan originations; the FHA/VA programs account for another 27% of originations. Major legislation is not likely before 2014, meaning the earliest timeframe for new regulations would be 2016, with implementation in 2017. The favored option right now is "Treasury Option 3," envisioning a large number of small securitizers (20). Fannie Mae and Freddie Mac likely will start paying down their government debt in 2013, which may reduce the perceived need for legislative reforms.

A second panelist agrees that housing legislation is not likely to occur until after the next presidential election; a third says that, while the structure of the housing market is not likely to change, it may become smaller as foreclosures and falling real estate prices put downward pressure on the rate of homeownership.

Another panelist focuses on regulatory changes already in the works, like Reg AB2 (21) and consumer protections laws that make a difference, even without overall structural reform. Another described a recent proposal for a trading market for first-loss pieces of residential mortgage loans (it sounds somewhat like the trading of the unguaranteed portions of SBA loans).

***Reducing the role of the GSEs:*** One panelist says competing proposals for housing reform span a range of degrees of privatization of the secondary mortgage market. Treasury Option 3 is a fully nationalized model with catastrophic backstop from the federal government and highly regulated entities providing the first loss insurance. At the opposite end of the spectrum are proposals that would wind down the GSEs over a number of years and make the market entirely private. An intermediate option might be to transfer risk with credit default swaps or similar arrangements. A second intermediate option might be to retain the GSEs, but with a smaller role and to create securities that use the senior-subordinated structure for credit enhancement.

The existence of the GSEs arguably helped to prevent or reduce the impact of asset bubbles. Before the creation of the first GSE in the midst of the Great Depression, asset bubbles were more common and had damaging effects. All the proposals for reducing the role of the GSEs would increase mortgage credit costs and would likely decrease home prices. he proposals at the extremes might promote the mispricing of credit risk.

Another panelist asked about the sectors of the mortgage market in which the GSEs should participate. Should the GSEs participate in both the affordable housing area and in the mainstream area? Some proposed conditions to restart the private-label MBS market:

- Regulatory rules must be finalized: risk retention and definition of qualified residential mortgage (QRM);
- Securitization must be economical (relative to holding loans on-balance sheet);
- Rating agencies must regain credibility, better transparency may help, and new entrants may help;
- Government standards need to be set, considering potential conflicts of interest;
- Credit standard need to be wider;
- Origination expertise must be developed for the private-label market;
- Underwriting should be done using a variant of the GSE underwriting system; and
- Title perfection, credit approval, and documentation processes have to be rebuilt.

One panelist says rating agencies will have a role in the revival of the private-label MBS market, arguing that rating agencies should take notice when a deal includes "super senior" tranches. The creation of such tranches may indicate market skepticism about the creditworthiness of the junior tranches that receive "AAA' ratings.

***Slow refinancing:*** One panelist says the currently slow pace of refinancing is really a credit issue. Affordability is high for distressed properties, assuming the buyer can make a 20% down payment. However, nondistressed properties are not especially affordable, even at current low interest rates. In addition, the standards for qualifying for a mortgage are quite tough, preventing homeowners and potential homeowners from getting loans, and the underwater status of millions of loans impedes refinancing of that cohort.

The HARP program would help borrowers on underwater loans to refinance into new loans with lower interest rates that would reduce default risk. The issue, however, is who should take the risk on the new loans? The loans arguably should not go to the GSEs because that would increase their risk.

A step to make the HARP program more effective would be to raise the current 125% LTV ceiling. Another step would be to skip doing appraisals and to instead just rely on AVMs. Another step would be to waive representations and warranties (i.e., rely on the representations and warranties on the predecessor loans) in securitizing modified loans. HARP has reached 800,000 borrowers, far less than the target number of 3 million to 3.5 million.

***Ginnie Mae:*** One panelist notes that recent originations of conforming loans have had LTVs in the md-60% range. Ginnie Mae currently absorbs the major share of purchase-money loans, while Fannie Mae and Freddie Mac account for a larger share of refinancing loans. Another panelist adds that the Ginnie Mae multifamily programs are very important. A third panelist adds that government housing policy needs to be explicit and on the government budget. FHA/VA loans have become the "lender of last resort."

***Homeownership:*** One panelist expects the rate of homeownership to decline. The rental market is not just multifamily buildings. It includes many single-family (One- to four-family) properties. There is institutional activity in buying up pools of single-family properties for rental. A policy initiative to amplify institutional interest in buying bulk quantities single-family homes could accelerate recovery in the residential real estate sector.

One panelist observes that other countries have had trouble with housing bubbles. He asserts that a high rate of home ownership may be a factor that promotes the formation of housing bubbles. Germany has a relatively low rate of homeownership but a generally strong economy. One panelist argues that it will take two things to fix the housing market: Close the supply-demand gap, and allow modifications.

## CLO 2.0: Market Lessons and Future (2:10pm)

One panelist observes that it is an interesting time to talk about CLOs. Several years ago the mood was quite different. CLOs today have some brighter spots than they did a few years ago, along with some challenges.



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A second panelist highlights the recent challenges: European sovereign debt worries, high unemployment in the U.S., and the tsunami in Japan several months ago. Spreads have widened in the CLO sector over the past several months. However, CLO equity has been trading actively. Important CLO performance measures, such as the proportion of portfolios in triple-C-rated assets, have been improving. CLO managers have been able to execute trades to improve par and to get more yield. Equity investors are getting returns of 30%, compared with 21% before the crisis. Leveraged loan quality has been improving. CLO issuance has been about $8 billion so far this year.

A third panelist agrees that the CLO market is showing signs of significant strength, estimating total issuance for the sector may reach $12 billion and 30 deals for the year. Looking back over history, CLOs have been a well performing asset classes and have weathered past economic downturns; the panelist says the reason behind the sector's strong performance is the fundamental credit analysis performed on the underlying loans. Current conditions in the leveraged loan space reflect the strong liquidity in the corporate sector and the strength of covenants in loans.

A fourth says CLO managers have generally been able to "beat the market" in terms of avoiding credits that ultimately defaulted. CLO investors can be happy with lower leverage in newer deals (i.e., higher credit enhancement levels) and shorter reinvestment periods. Equity from some old CLOs is attractive because those deals have higher leverage and the interest rates on their debt tranches is very low. Some new CLOs are being done with one rating.

Another panelist says equity in recent CLO transactions has been more broadly distributed than in deals from 2010. Also, some new CLO deals are being done with no warehousing. That is, the manager acquires the entire portfolio between the pricing and closing of the CLO.

***CLO documentation:*** Another panelist observes that new CLOs have better documentation. For example, new deals better address the issue of loan extensions than older deals did. He asserts that CLOs "did OK" (i.e., they performed as they should have). Another panelist notes that many areas of securitization adjusted documentation in the aftermath of the crisis, fixing issues like voting rights and clarifying that an issuer/manager does not have the right to cancel notes. In general, the quality of CLO documentation has improved because transaction parties pay more attention to documentation.

New investors have entered the CLO sector. Investors are more sophisticated than they were in the past and they often specify stipulations with respect to attributes they want in CLOs. Investors at the opposite ends of a CLOs capital structure may focus on opposite factors.

***CLO warehousing:*** Warehousing is a key issue for the CLO sector. Earlier in the year bankers would supply warehouse facilities for CLO managers. Some of the facilities were multiyear facilities that functioned like mini-CLOs. Now bankers are reluctant to provide warehouse facilities. Managers cite warehousing and the ability to place equity as the two biggest issues in working with banks. The risk of market value volatility is a tough challenge for warehousing.

***CLO managers:*** One panelist offers mixed views about the significance of managers as a factor in the creditworthiness of a CLO. Some managers clearly have had a positive influence on credit quality, while others have had the opposite effect. The most important thing for a CLO investor is to understand the management style of a CLO manager. The addition of clear prohibitions on note cancelations was a response to such behavior by a manager. Similarly, an investor needs to understand whether a manager is likely to extend loan maturities past the maturity of the CLO through which it is funded. There has been consolidation among CLO managers as larger ones absorbed smaller ones.

***Zing 7 litigation (22):*** In August, the Bankruptcy Court for the district of New Jersey denied a motion dismiss an involuntary bankruptcy proceeding against a CLO issuing entity domiciled in the Cayman Islands. The litigation is known as the Zing 7 case because the entity is call Zais Investment Grade Limited VII. Senior noteholders brought the petition but the junior noteholders objected. The junior noteholders asked the court to abstain from interfering in the Cayman entity. The court rejected the junior noteholders' argument. The court ultimately did not address a second argument that the senior noteholders were not qualified to bring an involuntary petition because they held only non-recourse debt. The court bypassed the non-recourse debt issue based on the fact that the debtor/issuer had failed to contest the petition within the prescribed time. One of the takeaways is that CLO documents arguably should include a provision requiring the issuer to contest the petition. Also, the deal did not include a non-petition covenant from the senior note holders, but the omission of the provision was inadvertent. Another panelist notes that the Zing 7 deal was in default and that it was not a true CLO because it had underlying structured finance collateral. He notes that it would be too dangerous for an investor to bring an involuntary bankruptcy petition on a non-defaulted CLO because of the risk of damages in the case of an adverse ruling.

***SEC Conflict of Interest Rule (23):*** The SEC issued a proposal for conflict of interest rules. The comment period ends in December. The rule would apply for one year after the closing of a deal. The rule is supposed to prevent conflicts of interest between parties to a securitization and investors in the deal. The focus is on whether a securitization participant would benefit from the adverse performance of a deal that sold to the investor. Another regulatory issue is risk retention (24). There are tax proposals that would create withholding tax risk. The SEC's proposal to amend Regulation AB (25) would impose onerous disclosure requirements. The industry tried to argue for a disclosure exemption.

***Article 122a (26):*** The risk retention in Europe is clogging CLO issuance. One panelist explains that Moody's intends to refrain from changing its methodology for rating CLOs. The methodology changes in June were the result of an extensive study and testing. Moody's would not plan to make further changes to the methodology simply because of double-dip recession. Panelists reiterate that the CLO sector has performed well and that investors should differentiate it from CDOs of ABS, which performed very poorly.

### Student Loan ABS: FFELP And Private Loans, Recent Developments, And Trends (3:05pm)

***Private student loans:*** One panelist observes that origination of private student loans has increased slightly from the trough of recent years. Underwriting standards are tough. All lenders are going after Ivy League students with co-signers who have high FICO scores. The proportion of loans to borrowers with FICO scores below 670 has declined. The low level of originations is more attributable to constrained supply than to weak demand. A second panelist notes that borrowers are being conservative in their borrowing and that they have many choices for structuring their educational borrowing (once they have qualified to borrow in the first place). A third panelist remarks that changing securitization practices, such as higher credit enhancement levels in securitizations, are all positive for investors.

One panelist says there continues to be material risk in private student loans because students face difficult job prospects once they graduate. A second panelist agrees risk on private student loans remains high. Conditions in the labor market affect not only the students but also the co-signers. Willingness to pay is not the primary issue; ability to pay is the main story. A third suggests that a good strategy for underwriting individual loans is to focus on the trend of a borrower's borrowed balances and the trend of his credit score.

One issue in underwriting student loans is preventing "over borrowing." Student loans have a public policy purpose (i.e., promoting higher education). The U.S. is sixteenth in the world in terms of degree attainment. That means that U.S. education policy should be pushing kids to go to college. However, budget issues have led 28 states to cut funding for education. This leads state schools to want to increase their enrollment of out-of-state students who must pay higher tuition. The average net tuition at a four-year college is $16,000. The maximum amount of a Federal Direct Loan is $5,500 and the maximum amount of a Pell Grant is $5,500. This leaves a $5,000 gap.

Banks can fund student loans with deposits. Other lenders can get warehouse lines from banks. Non-bank educational lenders should focus on having diversified sources of funding in order to avoid becoming overly reliant on any one source. One panelist observes that investors display a wide range of attitudes toward loans to students at vocational schools. Another panelist cautions that investors should be mindful of the differences between new vocational loans and the older ones that displayed very poor performance.

***Outlook for 12 to 18 months:*** One panelist predicts that performance of private student loans will continue to be weak for the next 12 to 18 months. The pricing of FFELP loans has changed with the termination of the FFELP program. Servicing transfers are an issue. Another panelist expects that there will be a continuing flow of deals backed by existing FFELP loans. Another investor notes that short-tenor ABS backed by FFELP loans have remained quite liquid, with tight spreads. The jury is still out on deals backed by private student loans. Fewer market participants are willing to do the analytic work on ABS backed by private student loans.

One panelist says that it is important for student loan servicers to work actively on managing defaults so that Congress does not step in and start trying to manage defaults itself. Another panelist argues that the student loan industry needs to reach out to investors and to win back investors' confidence by getting them comfortable with the loan programs, rather than focusing on the lenders or on the structures.

One panelist expects spreads on ABS backed by FFELP loans to be flat in the near term but to tighten in the longer term (but not to pre-crisis levels). Secondary trades are attractive because investors can achieve wider spreads. Another panelist states that there likely will be attractive opportunities for investors who focus on the student loan ABS sector.

Another panelist notes that prepayment trends on FFELP loans have followed the condition of the general economy. Prepayment speeds are currently slow, reflecting weak economic conditions. A different panelist remarks that in the private loan sector delinquencies are high and prepayments are virtually zero.

Servicing is a much less sensitive issue for FFELP loans than for private student loans. Small servicers can pose a credit quality issue for securitizations backed by private student loans. Solutions can include having a deal's trustee or a third party serve as a backup servicer.

Non-profit student loan lenders still have a large volume of auction rate securities on their books. One panelist asks why they have not done more restructurings of those securities. Another panelist replies that the issue is spreads. During the height of the financial crisis, some of the auction rate securities traded at prices in the 70s. Now they command prices in the 90s.

Is risk retention an issue for the student loan market? Issuers already hold more than 5% in most securitizations of private student loans. However, that is not true of securitizations backed by FFELP loans.

## Tuesday, Oct. 18, 2011

### The U.S. Macroeconomic Outlook: Senior Economist Roundtable (9:00am)

One panelist contends that the "stall speed" for the U.S. economy is a growth rate of roughly 1%. Earlier in the year, the growth rate dipped below 1%, which suggested a sharply increased likelihood of a recession. However, growth has recovered somewhat and the risk of a double-dip recession appears diminished. Other economic indicators are at anemic levels, but not so low as to signal recession. The other panelist remarks that the U.S. has been in recovery since 2008Q3, but the recovery has been very weak. The weakness of the recovery is a reflection of the type of recession that occurred. It was a debt-driven recession, which generally would not be followed by a vibrant recovery because consumers are cautious and consumer-spending remains muted.

***U.S. exposure to Europe:*** One panelist observes that the U.S. equity markets have displayed notable volatility in response to developments in Europe. Europe is the world's second largest economy and it is likely to go into recession. He argues that one of the main effects of European problems is how they affect sentiment in U.S. market participants. The other panelist observes that the problems in the Euro-zone are concentrated in the "olive belt" (i.e., southern Europe: Greece, Italy, Spain, and Portugal). The French and German economies are strong. However, the French and German economies have very large exposure to the olive belt. He asserts that there is no way for Greece to repay its debt and that the issue is not whether Greece will default but rather how its default will be managed. A European sovereign default would likely have a greater effect on financial markets than on the real economies of other nations.

There are interesting parallels between the Spanish housing bubble and the U.S. housing bubble. A key question, however, is who is holding the Spanish mortgage loans that are destined for default. There are currently huge numbers of empty condos on the Spanish seacoast. Moreover, Spain's unemployment rate is over 25%, adding to the mounting default risk.

One panelist asserts that reading the economic variables is difficult. Consumers still expect home prices to drop. Consumer confidence is very weak. It is not clear how much deleveraging will be enough. The other panelist argues that confidence is returning. Consumers who have jobs expect to still have them next year. The main issue is the level of debt. The consumer saving rate is currently around 5%. Before 1990, the consumer saving rate was 9%. At the household level, Americans should be saving more. However, at a societal level, what America needs is more consumer spending, rather than less. If the saving rate were to return to 9%, we would need to adjust to an economy where consumer spending accounts for only 67% of the whole economy, rather than 71%.

One panelist focuses on how household income levels have eroded. Unemployment is a major factor. The low interest rate environment has not produced a strong wave of mortgage loan refinancing because of negative equity, under-employment, and second-lien financing.

***Monetary policy:*** Monetary policy has little room to be effective. Interest rates are already so low that further meaningful reductions are not possible. "Operation twist," in which the Federal Reserve attempted to bring down long-term interest rates to spark mortgage refinancing was not effective because of the factors noted above. The next natural step for monetary policy would be through the exchange rate. However, other currencies are very weak right now so depreciating the currency is not a practical option. Thus, monetary policy is now largely ineffective.

***Fiscal policy:*** One panelist remarks that the key issue for fiscal policy is not whether to implement it but how. The other panelist asserts that the real challenge for fiscal policy is balancing the short-term against the longer-term issues. Short-term considerations argue that the government should be the "spender of last resort," to lift the economy out of recession. However, the ratio of debt to GDP is now about 70% and the annual deficit is about 10% of GDP. That means that it could take just two years for the U.S. to reach the danger level of a debt to GDP ratio of 90%. That means that the federal government really cannot afford to be the "spender of last resort." The problem with deficit spending as the main tool of fiscal policy is that the government did not accumulate a surplus during good times to be able to afford deficit spending during hard times.

***Mortgage distress:*** One panelist observes that the shadow inventory of distressed mortgage loans is gradually declining. However, it is still very large. He agrees with the view expressed on a previous panel that over a six year period the total number of loans/properties that experience distress will be around 11.5 million.

***The right amount of securitization:*** One panelist asserts that if America wants to retain the 30-year, fixed-rate mortgage then there will need to be a large volume of securitization to support that product. If America drops the 30-year FRM, then the domestic mortgage finance system might evolve to be more like the European system of shorter-term ARMs. The other panelist notes that the right level of securitization activity would be somewhat higher than the level today. Attendees at the conference generally express the view that the "right" level of securitization in the American economy would be less than it was before the financial crisis but significantly more than today's level.

***Euro:*** Disparate fiscal policies create major problems for the Euro-zone countries because they are forced to have a common monetary policy. The Maastricht Treaty sets fiscal policy and performance standards for the member nations of the Euro-zone but the requirements are more often ignored than observed.

## Piercing The Veil: Investors Speak Out On Transparency And Reporting (10:00am)

Three years ago, a survey of market participants indicated that the top factors for reviving the market were, in order of decreasing importance: enhanced disclosure and standardization of information; restoring confidence in the rating agencies; greater price transparency; better risk management; better alignment of incentives among stakeholders across the securitization chain; and changes to accounting rules and regulatory capital treatment.

One panelist focuses on price discovery. There is reasonably good price transparency on the senior tranches of consumer ABS. There is some price transparency on the senior tranches of CLOs. In contrast, price transparency on private-label MBS is weaker because pricing depends heavily on convexity. Also, pricing of many private-label MBS embeds macro outlooks. The bid side often reflects an apocalyptic outlook and the ask side often reflects a benign outlook (i.e., a low bid price based on a high loss scenario and a high ask price based on a low loss scenario). Another panelist observes that the TRACE system has added beneficial transparency to other sectors. He notes that certain investors, like mutual funds, need to get daily prices on their holdings but getting prices for many securitization products can be problematic.

***Servicing:*** One panelist observes that it is no easier today for an investor to decipher a remittance report than it was three years ago. Investors need to focus on the details of individual deals and on the differing abilities of servicers. For example, there is great variation among servicers in the proportion of their serviced loans that have been delinquent for more than 24 months. Likewise, there is material variation in servicers' modification practices. One practice, however, is reasonably uniform: upon modification of a loan, the servicer reimburses itself for outstanding advances. There is also substantial variation in the "stop advance" rate for different servicers. A high stop advance rate can cause severe extension of a deal's front-pay tranches and possibly expose those tranches to losses that they would otherwise have escaped. Another panelist counters that servicing issues and servicers' differing practices are reflected in the pricing of securities. He contends that investors receive appropriate compensation for the additional risk associated with particular servicers.

***Regulation AB update:*** One panelist favors the expanded disclosure under the proposed changes to Regulation AB. He favors a requirement to include all of a deal's legal documents in the required disclosures (27). He also favors the inclusion of updated loan-level details (28) and the inclusion of a computer model of a deal's cash-flow waterfall (29). He notes that inconsistent reporting practices in assets like private student loans make analysis difficult for investors. Student loan ABS servicers have differing practices in how they report voluntary prepayments.

Loan level information is available on many U.S. MBS and CMBS deals. However, it is not yet the norm for consumer ABS. Updated FICO scores for consumers are highly informative for predicting delinquencies, but the data is expensive. A requirement to supply that data might be too onerous because of the cost. One panelist remarks that it takes more than "a good story" to sell bonds today. The panelist asserts that investors feel that they were misled several years ago. They now insist on getting the data. The panelist asserts that loan level data is not necessary for ABS backed by credit cards or auto loans, but that it is necessary for private student loans and esoteric asset classes.

***Consumer privacy vs. Investor data demands:*** One panelist asserts that it should be the responsibility of a data provider to package data in a way that protects consumer privacy. Investors should not be ones to handle the consumer privacy issue. Another panelist expresses skepticism about issuers and servicers who use the consumer privacy issue as an excuse for not providing information to investors.

***Transparency of the rating process:*** One panelist notes that although many market participants say that they do not use ratings, everyone uses ratings to help with pricing bonds. A rating gives an indication of the general range of pricing for a security. Traders will always use a low rating to justify a low bid on a security. As an investor, it is very helpful to have more than one rating agency on a deal, especially on esoteric assets. It was a big issue earlier in the year when Standard & Poor's withdrew its preliminary rating on a CMBS deal after the deal had priced but before it had closed.

Another panelist notes that Standard & Poor's has made significant changes in its rating criteria over the past several years and that the firm tries to deliver more transparency through criteria articles. The withdrawal of the preliminary rating on the CMBS deal earlier in the year was a reflection of proper checks and balances operating in the process. The firm provided transparency about the actions it was taking and the reasons for those actions.

A third panelist remarks that many investors continue to place excessive reliance on ratings. Overreliance on ratings is a major issue. Fixing the issue will require investors to do more analysis themselves.

The securitization industry has the burden of demonstrating to the broader fixed-income community that securitizations are reasonable investment products in which they should be willing to become involved. One panelist feels that the key obstacle to the revival of the market is cleaning out the shadow inventory of distressed mortgage loans.

### Keynote Address, Joe Nocera, The New York Times (11:00am)

We are now several years past the financial crisis and its origins have been thoroughly explored. The tougher challenge is understanding where we are today and where we are going. Partisan politics is a terrible obstacle to progress. The recent U.S. budget crisis was a horrible example of a self-inflicted injury produced by partisan politics.

***Banks and Europe:*** In the early phases of the financial crisis, the actions to shore up the financial sector were wise policies. If the financial sector had collapsed, it could have produced a depression much worse than the recession that actually occurred. Indeed, in the years since the crisis, the U.S. banks have increased their levels of capital. The story in Europe is somewhat different. The banks have not done as much to increase their capital. The stress on the European sovereigns and the weak capital levels of European banks create a vicious cycle. European sovereign defaults would likely have much worse effects on the U.S. than did the Lehman bankruptcy.

***Fiscal policy:*** The U.S. does not really have a fiscal policy. There is monetary policy, and it is as aggressive as possible. The reason that there is not a fiscal policy is that Democrats and Republicans have sharply differing views. The debt crisis was fundamentally a dispute about fiscal policy. The Congressional "super committee" charged with crafting a solution to the deficit may have an impossible task. Republicans threatened to reject any proposal that includes tax increases. The Administration has threatened to veto any proposal that does not include tax increases. If there is no agreement, Draconian results happen automatically.

***Regulatory responses to the financial crisis:*** The Great Depression of the 1930s sparked a huge wave of new regulation. It produced the Glass-Steagall Act, the FDIC, the SEC and other huge reforms. The policy/regulatory response to the Great Depression was huge and radical. By contrast the response to the recent financial crisis was puny and overly complicated. It did not try to fix the regulatory jumble of bank regulators. It did not outlaw swaps, derivatives, or credit default swaps, but it did try to create a regulatory regime to make them less dangerous. It created the Consumer Financial Protection Bureau (CFPB), but that agency has not yet become a significant factor. Additionally, just a few months after the enactment of the Dodd-Frank law, Republicans took control of the House of Representatives and have started to gum up the works of the regulatory machinery. This has created greater uncertainty, which is retarding the recovery.

Neither political party has yet come to grips with the issue of housing. The Treasury released a white paper with three options (30). Loan modification programs have been ineffective. Republicans have taken the position that the only way to deal with Fannie Mae and Freddie Mae is to put them out of their misery. That view is not realistic. The federal government has been in the housing market since the 1930s. The idea of eliminating the GSEs and still having a healthy housing market is utterly absurd. A realistic housing policy with strong bipartisan support is one of the things that Washington could do that actually would help to support a strong economic recovery.

***Consumer finance protection bureau:*** The CFPB is a hot issue. Elizabeth Warren became a lightning rod for the Republicans. The Republicans were trying to prevent the CFPB from actually functioning by preventing the appointment of a director. The Republicans want to force a change in the underlying legislation, but that is unlikely because it would take 60 votes in the Senate. Because of the Republican opposition to her appointment as the CFPB director, Elizabeth Warren has become a "regulatory rock star." She is running for the Senate and has a pretty good chance of winning.

As long as the CFPB has a director, it can regulate what exists. It can take over the consumer protection functions from the federal bank regulators. One of the problems that led to the crisis was that regulated lenders allowed their practices to erode in order to compete with unregulated lenders. Under the current legislation the CFPB does not yet have authority over unregulated lenders.

***Too big to fail:*** The FDIC now has the power to wind down both banks and large finance companies. The Volker rule is supposed to make banks safer by not allowing them to trade for their own accounts. Despite the new legal regime, nobody knows whether the government would actually allow a "TBTF" (to-big-to-fail) institution to fail.

***Derivatives:*** Dodd-Frank requires the use of clearinghouses and exchanges and calls for improved transparency. The problem is that creating effective regulation for the derivatives sector is difficult. Some of the professionals who had worked to prevent regulation of the derivative markets in the 1990s and 2000s now take the opposite view. Producing transparency in the derivatives arena is very expensive. Large institutions may be able to bear the cost, but it might crush smaller market participants.

More than any specific regulatory changes, the partisan nature of American politics is the greatest challenge. America desperately needs a fiscal policy to align with the monetary policy. American business needs regulatory certainty. Absent radical change, America will potentially muddle along with an impaired economy for many years. The economy is not likely to collapse. A key factor is the euro crisis. America needs a lower corporate tax rate with virtually no loopholes. We got close to that in 1986, but it has been badly eroded by the subsequent creation of new loopholes.

### Finding Relative Value In The ABS Markets: Research Analysts' Roundtable (2:15pm)

***The outlook for consumer credit:*** Most panelists expect to see good performance from the average consumer in the consumer credit space. They cite more conservative debt trends for US consumers and a saving rate around 5%. Moreover, debt ratios are at 1999 levels. Year-over-year bankruptcy rates are under 10%. In particular, the auto loan market has been strong and lenders have not given up their underwriting standards; today's FICO scores are higher than in 2006, on average. Auto loans account for about 60% of the consumer debt market.

One panelist asserts that if we have another recession we would see deterioration from the current state. However, another credit cycle would show better performance in the consumer credit sector because there is less demand from the weaker credits. Overall, the panelist expects about 4% to 5% growth in consumer credit.

Spending has persisted at high levels but there's evidence that people are maintaining that spending level by not paying their mortgages. Cards and auto loans are higher on the priority of payments than mortgages, allowing people to live rent-free. This is evident in the growing number of strategic mortgage defaults. People with higher FICO scores are more likely to exercise strategic defaults. Currently, about 14% of total delinquencies are tied to these borrowers. One panelist suggests that strategic default reduces a borrower's credit score by about 100 points.

***The expectation for supply:*** Some panelists see continued growth in securitization. One panelist expects over $60 billion in auto ABS this year, claiming that ABS remains the cheapest source of funds for financing. Another panelist says that auto loan volume is up around 11%, and expecting strong issuance in 2012; the panelist expects about 13 million units will be sold and indicates that auto makers are making money.

Cards have not been as robust. Banks may be mistaken by not issuing more cards. The supply of new credit cards for securitization for 2012 is not large. Student loan volume is flat year to date. "Other" consumer credit issuance is about $6billion to $10 billion also flat, year over ear. One panelist expresses caution and does not expect a lot of growth as consumers deleverage, hence not a lot of ABS issuance. Banks may look oversees, to Australia for example, for ABS investment.

#### Esoteric assets:

Market participants are seeing some interest in the esoteric space for "new" assets, but the "benchmark" asset classes remain the strongest. As the credit card sector shrinks, there will be a shift into more off the run sectors. Well-structured good performing assets will provide better relative value.

***Investor participation at the current low spread levels:*** Investor interest in ABS in light of the relatively low spreads is generally a function of several factors. Investors use ABS as a cash surrogate--these are "true" 'AAA', as opposed to others that are derived 'AAA'. Liquidity in the 'AAA' auto ABS and card ABS are important. There is no need for banks to deleverage from this asset class. ABS have the lowest spreads and better returns because they're short term and of high quality. One panelist points out that we would need a shift in interest rates to draw funds out of the ABS market.

***ABS collateral performance:*** The market is very strong now with very low charge off levels, even better than pre-crisis levels. In spite of the weak economy, the panelists expect continued good performance. They believe credit enhancement levels are sufficient.

***Adequacy of credit enhancement levels:*** The panelists believe that although the credit rating agencies missed in some other sectors the credit enhancement levels in ABS are appropriate and the ratings have been stable. However, the credit rating agencies have gotten more conservative, driving up the credit enhancement levels. One panelist believes the credit enhancement levels are a bit high.



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Cards performed well through the crisis because banks infused credit enhancement. Banks may not have needed to further enhance their deals, and may try to press for lower enhancement in the future. While levels have gone up, some issuers with very low historical losses have cut credit enhancement to below pre-crisis levels. Investors prefer higher credit enhancement.

One panelist highlights that although the credit rating agencies generally got it right in ABS, the regulators took a broad brush in their reaction to the crisis. The regulations should be more discriminating based on the sector specific experience. There is some concern over the apparent pro-cyclical credit rating agency approach whereby credit enhancement fluctuates and deals get caught short when things turn. Investors prefer a more stable level of credit enhancement.

One panelist expresses the view that investors should be more vigilant about changes in credit enhancement levels. The panelist states investors should "put their foot down," about credit enhancement levels when considering purchasing structured securities, and refers to the GS CMBS deal where investors demanded more credit enhancement.

***Relative value in CLOS:*** Recent observations show dollar denominated issuance activity in Europe. The European mortgage market doesn't see strategic defaults primarily because of full recourse to the borrower. Since Europe is an ARM market, there's less need or desire for refinancing. However, CLOs are a different story. Consumer ABS is much more liquid than CLOs. There's some uncertainty in CLO 'AAA's and as a result investors demand higher premiums. Rating performance in CLOs has been good, and 'AAA' CLOs are a good pick-up.

***The treatment of the US 'AA+' in ABS:*** The panelists question the appropriateness of Standard & Poor's 15% haircut on the U.S. guarantees in ABS. One panelist challenges the approach stating there's no quantitative reasoning for the 15% haircut.

***Recommendations:*** The moderator asks the panelists to share their recommendations. Their preferences include:

- 'AAA' off the run sectors across borders, and prime auto.
- CLO and U.K. Prime RMBS.
- Subordinate auto ABS, and select subprime auto ABS; dealer floor plan; and private label cards.
- Last cash flow A4 auto ABS because they are getting extra spread.

The panelists all agree that investors cannot ignore credit ratings.

### TRACE For The Structured Finance Market: Impact Of Price Reporting On Trading Strategy (3:05pm)

TRACE was expanded in May 2011 on a provisional basis to collect data on ABS and RMBS security trades. At the conference, FINRA announced a joint initiative with Interactive Data Corp. for providing the market with a set of U.S. Structured Trading Activity reports.

***Overview of TRACE:*** The panelists share their views on how this system is likely to work in a market where each security, even in the same asset class, is likely to be somewhat different. The differences arise from each transaction's structural features, collateral composition, and collateral quality. While TRACE will not report activity if the number of trades is small, there was the concern that providing trading information without detailing the motivation behind the trades could cause the market to react in both positive and negative ways.

Overall, the panelists express generally positive sentiments on the initiative, asserting that in the long-term this will be good for the market and will help with transparency. In the short-term however, they caution that the market must exercise caution in interpreting the data and in applying the data to their specific securities.

### RMBS Traders' and Researchers' Roundtable (3:05pm)

***Over- and under-valuation in the market:*** There is quite a bit of overvaluation in the market, according to one panelist. Non-agency RMBS is down by 39%. Price is bi-furcated by type and capital structure. There has been a huge deterioration in prices in the past six months. Subprime securities that were trading in the 40s are now trading in the 30s or lower. Default and loss expectations are being priced in but the pricing excludes the impact of servicers not advancing and loan modifications.

One panelist associates this entire price shift to the shift in the forward curve. The rapid drop in the 10-year point on the forward curve from 3.40% to 1.80% caught traders off guard. The present value of this downward shift of the forward curve over the next 20 years accounts for the price drop from the 40s to 30s. People got caught on the wrong side when Operation Twist was announced. This downturn was furthered by the near default of the U.S. government, by the economists announcing the economy's dip back into recession, and developments in China.

***Policies that can help:*** One panelist suggests we need two types of policies: we need principal write-downs to bring the market in line. Principal modifications are more effective in resolving issues. While principal modifications cause moral hazard, this panelist feels a way around the moral hazard is through a shared appreciation feature. After a modification, the lender would share in any upside.

Another panelist believes investors buying properties for rent can help the mortgage market. If investors could execute large bulk purchases, they could make an impact by providing large-scale principal write downs. Policymakers should allow bulk purchases to large-scale investors and then provide financing to them for these purchases.

***Pessimism given collateral performance outlook:*** The moderator asks the panel if they believe there is too much pessimism in the market given the outlook on collateral performance. The general sense is that the view is too pessimistic given the collateral outlook. Roll rates for subprime loans with combined loan-to-values (LTVs) greater than 100% have been improving--i.e., credit has improved for these borrowers. However, borrowers with loans with combined LTVs below 100% have not been able to prepay.

***Default expectations and trend:*** As a trader, it is necessary to look at all the scenarios that the market presents and then consider the possibilities, and make a smart choice. Given the trends, it is hard to believe that a borrower who has paid for five years still has a 50% chance of default. There is a shifting focus to yields and the types of buyers in the market (i.e., buyer base).

Loss severities are very important. One panelist's best guess is that severities will go up a little more before coming down. As timelines extend servicers will stop advancing--subprime current timelines are about 32 months to liquidate, and expected to go to 48 months. Therefore, advances should slow down significantly. Fewer advances in theory make severities decline but the impact on the investor is uncertain. The LTV of what is liquidating now is higher than the LTV of what is not currently liquidating. This should lead to lower loss severities in the future. Estimating losses on what has been observed in the last six months may yield different results in the future. Investors are making market plays based on severity differentials.

***Outlook:*** The panelists provide their views for the market; each of their responses follow:

- Slow pay collateral subprime and pay option ARMS. Bonds where future loss severity is expected to be lower than in the past. Consider the worst the servicer can do and still get a good yield 10 to 11%, with a 7% worst-case yield, in a 2% market.
- Another panelist is bearish in the short term but not so bearish on supply.

- Second-pay subprime mezzanine tranches with a lot of total rate of return. Prime hybrid. Expects higher CDRs that will spook investors and impact the price.
- There is nothing on the horizon to close in the yields near term. Likes second and third sequential pay bonds, and 2006 and 2007 deals. The cost to rent for many borrowers provides a disincentive to default.
- Likes Alt-A over the other sectors. Fixed with fixed collateral. Negative on subprime, and 2006 and 2007 prime has potential risks.
- Seasoned subprime 2002, 2003, and first half 2004. Very bullish on the sector. These borrowers have equity in the loans; because they don't have piggyback loans. They put down 20% in real money. Paying 10% principal a month.
- Front-end prime and seasoned subprime.

Every speaker has a different preferred sector, showing that a trader has many opportunities to find value. As in the opening session on Monday, one panelist asked the audience--"how many investors in the room," some; "how many are looking to buy," very few; "how many are looking to sell," fewer still. Most investors did not respond either way, indicating they are not ready to bring new money into RMBS, reinforcing Monday morning's sentiment.

The session ended with a heated debate over people walking away from their loans rather than living up to their obligations. Some panelists argue that lenders should take a heavy hand with defaulted borrowers, pushing the bad loans out of the system, letting the market hit bottom as soon as possible. That would lead the way to a quicker recovery. Most panelists argued the alternative view: push principal modifications, and other interventions to save the borrowers, ironically, prolonging the market dislocation, and extending the time to recovery.

**Endnotes:**

(1) Olorunnipa, T., Housing Hangover, The Miami Herald at A1 (Oct. 16, 2011) http://www.miamiherald.com/2011/10/15/2456154/shadow-inventory-of-homes-could.html

(2) Securities and Exchange Commission, Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Release No. 34-63751, 76 Fed. Reg. 4489 (Jan. 26, 2011) (final rule)

(3) Department of the Treasury-Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, Federal Housing Finance Agency, Securities and Exchange Commission, and Department of Housing and Urban Development, Credit Risk Retention, 76 Fed. Reg. 83 (April 29, 2011) (proposed rule).

(4) Directive 2009/111/EC, O.J. L 302/97 at 110 (Nov. 17, 2009) http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0097:0119:EN:PDF(adding new Article 122a to the Capital Requirements Directive)

(5) See e.g., Department of the Treasury-Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, and Department of the Treasury-Office of Thrift Supervision, Advance Notice of Proposed Rulemaking Regarding Alternatives to the Use of Credit Ratings in the Risk-Based Capital Guidelines of the Federal Banking Agencies, 75 Fed. Reg. 52283 (Aug. 25, 2010)

(6) Basel Committee on Banking Supervision, Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems (revised June 2011) http://www.bis.org/publ/bcbs189.pdf

(7) Basel Committee on Banking Supervision, Enhancements to the Basel II Framework (June 2009)

http://www.bis.org/publ/bcbs115.pdf

(8) Securities and Exchange Commission, Prohibition Against Conflicts of Interest in Certain Securitizations, Release No. 34-65355, 76 Fed. Reg. 60320 (Sept. 28, 2011) (proposed rule)

(9) Department of the Treasury-Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, and Securities and Exchange Commission, Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (Oct. 11, 2011) http://www.fdic.gov/news/board/2011Octno6.pdf

(10) See "Risk Retention", Monday, Oct. 17, 2011, above

(11) 15 U.S.C. § 78o-11(e)(4); 76 Fed. Reg. at 24117-24129 (April 29, 2011) (discussing alternative approaches to defining QRMs)

(12) 76 Fed. Reg. at 24148 (April 29, 2011)

(13) 15 U.S. C. § 78o-9, Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 § 939F, 124 Stat. 1376, 1889-90 (2010)

(14) Securities and Exchange Commission, Prohibition Against Conflicts of Interest in Certain Securitizations, Release No. 34-65355, 76 Fed. Reg. 60320 (Sept. 28, 2011) (proposed rule)

(15) Basel Committee on Banking Supervision, Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring (December 2010) http://www.bis.org/publ/bcbs188.pdf

(16) Basel Committee on Banking Supervision, Enhancements to the Basel II Framework at 3 (July 2009) http://www.bis.org/publ/bcbs157.pdf

(17) Directive 2009/138/EC, O.J. L 335/1 (17 Dec 2009) http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:335:0001:0155:EN:PDF

(18) Department of the Treasury-Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, and Securities and Exchange Commission, Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (Oct. 11, 2011) http://www.fdic.gov/news/board/2011Octno6.pdf

(19) Directive 2009/111/EC, O.J. L 302/97 at 110 (Nov. 17, 2009) http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0097:0119:EN:PDF (adding new Article 122a to the Capital Requirements Directive)

(20) Department of the Treasury and Department of Housing and Urban Development, Reforming America's Housing Finance Market – A Report to Congress at 29 (February 2011) http://www.treasury.gov/initiatives/Documents/Reforming%20America%27s%20Housing%20Finance%20Market.pdf

(21) Securities and Exchange Commission, Asset-Backed Securities, Release Nos. 33-9117, 34-61858, 75 Fed. Reg. 23328 (May 3, 2010) (proposed rule)

(22) In re Zais Investment Grade Limited VII, No. 11-20243 (Bankr. D.N.J. Aug. 26, 2011)

(23) Securities and Exchange Commission, Prohibition Against Conflicts of Interest in Certain Securitizations, Release No. 34-65355, 76 Fed. Reg. 60320 (Sept. 28, 2011) (proposed rule)

(24) See "Risk Retention", Monday, Oct. 17, 2011, above

(25) Securities and Exchange Commission, Asset-Backed Securities, Release Nos. 33-9117, 34-61858, 75 Fed. Reg. 23328 (May 3, 2010) (proposed rule)

(26) Directive 2009/111/EC, O.J. L 302/97 at 110 (Nov. 17, 2009) http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0097:0119:EN:PDF (adding new Article 122a to the Capital Requirements Directive)

(27) Securities and Exchange Commission, Asset-Backed Securities, Release Nos. 33-9117, 34-61858, 75 Fed. Reg. 23328, 23420 (May 3, 2010) (proposing to amend Item 1100(f) relating to the filing of exhibits)

(28) Id. at 23430 (proposing to add Item 1121(d) relating to asset level performance information)

(29) Id. at 23429 (proposing to add Item 1113(h) regarding requirement to supply cash flow waterfall program)

(30) Department of the Treasury and Department of Housing and Urban Development, Reforming America's Housing Finance Market – A Report to Congress at 29 (February 2011) http://www.treasury.gov/initiatives/Documents/Reforming%20America%27s%20Housing%20Finance%20Market.pdf