BFCSA

Banking & Finance Consumers Support Association (inc)

Help is at hand...

RMBS Research:

Background

http://www98.griffith.edu.au/dspace/bitstream/handle/10072/22360/50602_1.pdf;jsessionid=088D481EC12BA9914E5BEB8439B9BA6C?sequence=1

The first RMBS transaction was undertaken in 1977 by Bank of America, and consisted of a simple 'pass-through' structure.

Mortgage securitisation in Australia, plays an increasing role in mortgage finance, having a dramatic growth after 1997 particularly.

- Total securitisation outstanding surged from AU$ 2.05 billion in December 1988 to AU$ 142.26 billion in December 20031.
- Mortgage securitisation is the largest contributor for the increase, from AU$ 1.303 billion to AU$ 105.97 billon.
- This market ranked second to USA in size. Australian mortgage markets differ from USA in several ways.
- Since the earlier 1990s, mortgage corporations have been active, becoming major players in the securitisation market eventually. The Australian primary market is also quite unique.
- Four major commercial banks have traditionally dominated the market, with around 60% of market share of own-occupied home loans in 1994, and had some declines in recent years.
- More interestingly, nearly 80 percent of Australian mortgages are originated with adjustable rates.
- Any reductions in interest rate, therefore, have a greater impact on borrowers' costs because not only existing loans but also newly- originated ones are more sensitive to any rate adjustments.
- Since the early 1990s, securitisation has enabled mortgage corporations to establish in Australia and to securitise their loans (nearly 100%) in both the domestic and global capital markets for raising cheaper funds and then lending them to borrowers.
- The whole recycling process allows them to grow quickly and compete with the traditional lenders, such as commercial banks, by providing cheaper and new products (currently about 2,000 products in the market).

Australia Bureau of Statistics

http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features60March%202009

Definition:

- 'Securitised loans' are loans that have been converted to 'residential mortgage-backed securities' and sold to institutional investors via a trust or a company known as a special purpose vehicle.
- These loans generally have a higher risk associated with them. They currently make up around one-quarter of outstanding housing loans, with the remainder being on banks' balance sheets.

ABS Data:

http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features60March%202009

Issue 4102.0 - Australian Social Trends, March 2009

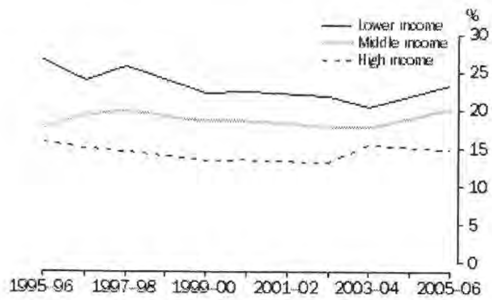
Debt Servicing:

The extent to which repaying their debt places a financial burden on households, in particular households with relatively low income:

- In 2005-06, there were 526,000 lower income households with a mortgage for owner occupied property, representing 23% of households in this income group.
- The median proportion of gross household income spent on mortgage repayments among lower income households decreased slightly in the ten years to 2005-06 (from 27% to 23%).
- However, there was a slight increase in the two years following 2003-04 from 20% to 23%, which may have been related to higher interest rates and house prices.
- Among these lower income households in 2005-06, 20% reported that they were paying between 30% and 50% of their gross household income on mortgage repayments and one-tenth were paying more than 50%.

Table: Weekly Owner Occupier % of Income as Mortgage Repayments

WEEKLY OWNER OCCUPIER MORTGAGE REPAYMENTS AS A PROPORTION OF WEEKLY GROSS HOUSEHOLD INCOME: INCOME GROUP(a)(b)



(a) Median proportion for each income group

(b) Lower income refers to households in the second, third and fourth equivalised disposable household income deciles; middle income to those in the fifth and sixth deciles, and high income to those in the ninth and tenth deciles

Source: ABS 1995–96 to 2005–06 Surveys of Income and Housing

Housing Loan Arrears and Securitisation

Another measure of the extent to which households are having difficulties servicing their debt is whether they are behind on their mortgage repayments.

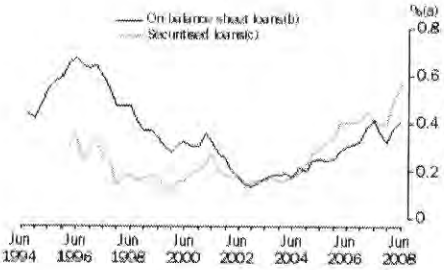
- From January 2001 to June 2008, the proportion of securitised housing loans more than 90 days in arrears increased from 0.15% to 0.35%.
- The arrears rate for prime securitised housing loans increased from 0.21% to 0.57% from January 2001 to June 2008. (Source RBA).
- From September 2003 to June 2008, the 90-day arrears rate for housing loans on banks' balance sheets (which account for around 75% of all outstanding housing loans) increased from 0.18% to 0.41%.
- For securitised prime low-doc loans, the arrears rate was 1.2% in June 2008, more than double that for securitised prime full-doc loans. The arrears rate for non-conforming loans was much higher at 8.5%.
- In September 2008 the Reserve Bank estimated that there were around 17,000

borrowers who were more than 90 days behind on their mortgage repayments, up from 15,000 borrowers in March 2008. (Source RBA).

- The easing of credit standards over the past decade has meant that many borrowers were able to obtain a housing loan who previously may not have been eligible, and many others have been able to borrow larger amounts. (Source RBA).

Table: Housing Loans 90 or more days in Arrears

HOUSING LOANS 90 OR MORE DAYS IN ARREARS



(a) Value of loans 90 or more days in arrears as a proportion of the value of all loans
(b) From September 2003 includes 'impaired' loans that are in arrears and not well secured by collateral
(c) Prime loans
Source: Australian Prudential Regulation Authority; Perpetual; Reserve Bank of Australia; Standard & Poor's

New South Wales

The overall arrears rate for prime securitised loans was higher in New South Wales than the other states and territories

- Arrears increased to a greater extent between April 2003 and July 2008 (from 0.18% to 0.84%).
- The 2004–2006 increase in arrears rates in New South Wales resulted in a sharp increase in the number of court applications for property repossession as a proportion of the dwelling stock, from 0.10% in 2003 to 0.22% in 2006 (steady at 0.22% in 2007).

RMBS's and the Australian Government

http://www.aofm.gov.au/content/publications/reports/AnnualReports/2008-2009/html/04_Part_2.asp

Background:

- Australian RMBS are high quality and there has never been a credit-related loss on a rated prime residential mortgage-backed security in Australia.
- The SPV is legally separate to the originator of the assets, and is structured to remain unaffected in the event that the originator becomes bankrupt.
- Subordination is the name given to the structure whereby the securities that are supported by the pool of mortgages are structured into 'tranches' that allow 'senior' notes to be repaid before the other 'mezzanine' and 'junior' or 'subordinated' notes.
- Occasionally, the AOFM has purchased small amounts of the most senior, fastest paying tranches (see class A-S in Figure 1 above), but these tranches have typically been purchased solely by other investors.
- The amount of subordination in the tranches below the AOFM's lowest-ranked investments has varied from 2.7 per cent to 9.4 per cent of the pool.
- Lenders mortgage insurance (LMI) is another common form of credit enhancement. LMI providers insure bondholders against defaults by mortgage borrowers.

- On 5 April 2011 the Treasurer issued directions that it will continue to invite the submission of proposals from arrangers of RMBS issues on a reverse enquiry basis for considering investment proposals.
- Proposals considered under this approach will be assessed against the objectives of supporting competition in lending for housing and small business.
- The AOFM will review its approach from time to time in the light of experience with the Program and changing market conditions. The AOFM is particularly mindful of its objective of encouraging a transition towards a sustainable securitisation
- The AOFM has decided to continue its current approach to investment in RMBS.

AOFM Annual Report 2011 Page 29
http://www.aofm.gov.au/content/publications/reports/AnnualReports/2010-2011/download/AOFM_Annual_Report_2010-11.pdf

Current RMBS Holdings:
http://www.aofm.gov.au/content/_download/statistics/overview/PortfolioOverviewJune2012.pdf

All figures ($millions)

31 Mar 2011	30 Jun 2011	30 Sep 2011	30 Dec 2011	30 Mar 2012	30 Jun 2012
10,345	**10,830**	**10,683**	**11,299**	**10,876**	**11,201**

Table: Aust Debt and Assets managed by AOFM:

Table 2: Australian Government debt and assets administered by the AOFM

	Interest		Book volume		Effective yield	
	2007-08	2008-09	2007-08	2008-09	2007-08	2008-09
	$ million		$ million		per cent per annum	
Contribution by instrument						
Treasury fixed coupon bonds	(2,947)	(3,182)	(48,476)	(56,514)	6.08	5.63
Treasury inflation indexed bonds	(593)	(687)	(8,317)	(8,677)	7.13	7.92
Treasury notes	-	(75)	-	(2,641)		2.85
Other miscellaneous domestic debt	(0)	(0)	(4)	(0)	8.22	7.20
Foreign loans (a)	0	(2)	(6)	(7)	-3.42	23.27
Gross physical CGS debt	(3,540)	(3,946)	(56,804)	(67,840)	6.23	5.82
Interest rate swaps	(180)	969	-	-		
Gross CGS debt (after swaps)	(3,721)	(2,977)	(56,804)	(67,840)	6.55	4.39
Term deposits with the RBA	1,197	981	17,378	19,759	6.89	4.97
Investments in bank paper	-	140	-	2,108		6.64
Term investments (b)	-	199	-	2,864		6.96
RMBS investments	-	89	-	1,859		4.80
State Housing Advances	171	166	2,899	2,826	5.89	5.89
Gross assets	1,368	1,576	20,277	29,416	6.75	5.36
Total debt and assets	**(2,353)**	**(1,400)**	**(36,527)**	**(38,423)**	**6.44**	**3.64**
Contribution by portfolio						
Long Term Debt Portfolio (c)	(3,727)	(2,690)	(56,892)	(62,070)	6.55	4.33
Cash Management Portfolio	1,204	1,034	17,466	18,961	6.89	5.45
RMBS Portfolio	-	89	-	1,859		4.80
State Housing Portfolio	171	166	2,899	2,826	5.89	5.89
Total debt and assets	**(2,353)**	**(1,400)**	**(36,527)**	**(38,423)**	**6.44**	**3.64**
Re-measurements (d)	(118)	(232)				
Total after re-measurements	**(2,471)**	**(1,632)**	**(36,527)**	**(38,423)**		

Table 5: RMBS Investments as at 30 June 2011

Table 5: AOFM's RMBS investments up to 30 June 2011

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class A1	0.7	1M BBSW + 1.25%	132.00
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class A2	3.5	1M BBSW + 1.50%	325.00
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class AB	5.0	1M BBSW + 1.80%	39.00
17-Nov-08	9-Dec-08	Members' Equity Bank	SMHL Securitisation Fund 2008-2	Class A1	2.8	1M BBSW + 1.30%	500.00
4-Dec-08	12-Dec-08	Challenger	Challenger Millennium Series 2008-2 Trust	Class A	2.8	1M BBSW + 1.35%	481.00
4-Dec-08	12-Dec-08	Challenger	Challenger Millennium Series 2008-2 Trust	Class AB	4.5	1M BBSW + 1.75%	19.00
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class A2	1.5	1M BBSW + 1.20%	250.00
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class A3	4.5	1M BBSW + 1.40%	204.75
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class AB	4.5	1M BBSW + 1.70%	15.25
6-Mar-09	26-Mar-09	CUA	Series 2009-1 Harvey Trust	Class A1	3.6	1M BBSW + 1.40%	350.00
13-Mar-09	18-Mar-09	Bendigo and Adelaide Bank	TORRENS Series 2009-1 Trust	Class A2	4.2	1M BBSW + 1.35%	475.00
23-Mar-09	30-Mar-09	AMP Bank	Progress 2009-1 Trust	Class A2	4.0	1M BBSW + 1.30%	425.00
3-Apr-09	21-Apr-09	Bank of Queensland	Series 2009-1 REDS Trust	Class A1	4.2	1M BBSW + 1.30%	500.00
9-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A1	0.1	1M BBSW + 0.90%	14.50
9-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A2	0.9	1M BBSW + 1.20%	164.70
9-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A3	3.2	1M BBSW + 1.40%	253.00
9-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class AB	4.0	1M BBSW + 1.65%	37.60
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A2	0.5	1M BBSW + 1.00%	38.20
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A3	1.5	1M BBSW + 1.30%	152.50
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A4	4.3	1M BBSW + 1.45%	289.00
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class AB	4.4	1M BBSW + 1.70%	20.30
11-May-09	14-May-09	Members' Equity Bank	SMHL Securitisation Fund 2009-1	Class A2	3.7	1M BBSW + 1.35%	500.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class A2	0.5	1M BBSW + 1.00%	10.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class A3	2.9	1M BBSW + 1.40%	435.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class AB	4.1	1M BBSW + 1.70%	13.80
1-Jun-09	5-Jun-09	FirstMac	FirstMac Mortgage Funding Trust Series 1-2009	Class A3	2.9	1M BBSW + 1.40%	456.00
1-Jun-09	5-Jun-09	FirstMac	FirstMac Mortgage Funding Trust Series 1-2009	Class AB	5.0	1M BBSW + 2.20%	40.62
9-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class A1	0.5	1M BBSW + 1.10%	16.00

Table 5: AOFM's RMBS investments up to 30 June 2011 (continued)

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
09-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class A2	3.5	1M BBSW + 1.40%	282.50
09-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class AB	5.4	1M BBSW + 1.60%	1.00
14-Jul-09	28-Jul-09	Australian Central Credit Union	Light Trust No. 2	Class A1	4.0	1M BBSW + 1.30%	190.00
20-Aug-09	04-Sep-09	Suncorp Metway	APOLLO Series 2009-1 Trust	Class A3	3.6	1M BBSW + 1.30%	499.20
28-Aug-09	11-Sep-09	Greater Building Society	GBS Receivables Trust No. 4	Class A1	4.3	1M BBSW + 1.35%	190.00
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class A2	1.0	1M BBSW + 0.90%	35.00
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class A3	3.3	1M BBSW + 1.40%	58.50
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class AB	4.0	1M BBSW + 1.65%	6.30
21-Oct-09	28-Oct-09	RESIMAC	RESIMAC Premier Series 2009-2	Class A2	3.3	1M BBSW + 1.40%	38.10
21-Oct-09	28-Oct-09	RESIMAC	RESIMAC Premier Series 2009-2	Class AB	3.8	1M BBSW + 1.90%	18.30
10-Nov-09	24-Nov-09	FirstMac	FirstMac Mortgage Funding Trust Series 2-2009	Class A2	3.5	1M BBSW + 1.40%	195.40
10-Nov-09	24-Nov-09	FirstMac	FirstMac Mortgage Funding Trust Series 2-2009	Class AB	5.0	1M BBSW + 1.95%	10.74
22-Jan-10	29-Jan-10	AMP Bank	Progress 2010-1 Trust	Class AB	5.2	1M BBSW + 1.80%	36.00
09-Feb-10	17-Feb-10	Bank of Queensland	Series 2010-1 REDS Trust	Class A	3.1	1M BBSW + 1.30%	250.00
25-Feb-10	10-Mar-10	CUA	Series 2010-1 Harvey Trust	Class A1	2.9	1M BBSW + 1.30%	143.00
05-Mar-10	15-Mar-10	Members' Equity Bank	SMHL Securitisation Fund 2010-1	Class A	2.6	1M BBSW + 1.35%	250.00
17-Mar-10	24-Mar-10	Bendigo and Adelaide Bank	TORRENS Series 2010-1 Trust	Class A	2.8	1M BBSW + 1.35%	123.00
26-Mar-10	31-Mar-10	IMB	Illawarra Series 2010-1 RMBS Trust	Class A	3.0	1M BBSW + 1.35%	157.50
12-May-10	17-May-10	RESIMAC	RESIMAC Premier Series 2010-1	Class A	2.4	1M BBSW + 1.65%	10.00
25-May-10	09-Jun-10	Suncorp Metway	APOLLO Series 2010-1 Trust	Class A2	6.0	1M BBSW + 1.10%	300.00
02-Jul-10	14-Jul-10	Members' Equity Bank	SMHL Securitisation Fund 2010-2E	Class A3	5.7	1M BBSW + 1.10%	250.00
08-Jul-10	20-Jul-10	Bendigo and Adelaide Bank	TORRENS Series 2010-2 Trust	Class A3	3.0	1M BBSW + 1.10%	19.50
08-Jul-10	20-Jul-10	Bendigo and Adelaide Bank	TORRENS Series 2010-2 Trust	Class A4	5.8	1M BBSW + 1.10%	476.50
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class A2	1.5	1M BBSW + 1.40%	20.00
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class A3	5.0	1M BBSW + 1.30%	139.25
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class AB	3.7	1M BBSW + 1.85%	10.75
11-Aug-10	18-Aug-10	Liberty Financial	Liberty Prime Series 2010-1	Class A2	3.3	1M BBSW + 1.25%	90.00
11-Aug-10	18-Aug-10	Liberty Financial	Liberty Prime Series 2010-1	Class AB	4.0	1M BBSW + 1.65%	10.40

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
18-Aug-10	27-Aug-10	Bank of Queensland	Series 2010-2 REDS Trust	Class A2	6.2	1M BBSW + 1.10%	497.50
26-Aug-10	02-Sep-10	Macquarie Bank	PUMA Masterfund P-10	Class A3	6.3	1M BBSW + 1.15%	247.50
06-Sep-10	09-Sep-10	FirstMac	FirstMac Mortgage Funding Trust Series 1-2010	Class A3	4.7	1M BBSW + 1.30%	164.00
06-Sep-10	09-Sep-10	FirstMac	FirstMac Mortgage Funding Trust Series 1-2010	Class AB	3.6	1M BBSW + 2.20%	26.77
23-Sep-10	28-Sep-10	Members' Equity Bank	SMHL Securitisation Fund 2010-3	Class A2	6.1	1M BBSW + 1.10%	200.00
14-Oct-10	20-Oct-10	ING Bank (Australia)	IDOL Trust Series 2010-1	Class A2	7.5	1M BBSW + 1.10%	250.00
10-Nov-10	18-Nov-10	Australian Central Credit Union	Light Trust No. 3	Class A3	5.4	1M BBSW + 1.20%	243.50
19-Nov-10	25-Nov-10	RESIMAC	RESIMAC Premier Series 2010-2	Class A2	4.8	1M BBSW + 1.25%	148.00
26-Nov-10	03-Dec-10	Police and Nurses Credit Socie	Pinnacle Series Trust 2010-T1	Class A2	7.2	1M BBSW + 1.25%	96.50
26-Nov-10	03-Dec-10	Police and Nurses Credit Socie	Pinnacle Series Trust 2010-T1	Class AB	6.7	1M BBSW + 2.00%	14.60
10-Dec-10	16-Dec-10	Bendigo and Adelaide Bank	TORRENS Series 2010-3 Trust	Class A5	4.6	1M BBSW + 1.10%	395.00
10-Dec-10	16-Dec-10	Bendigo and Adelaide Bank	TORRENS Series 2010-3 Trust	Class AB	4.7	1M BBSW + 1.80%	20.00
15-Dec-10	21-Dec-10	Wide Bay Australia	WB Trust 2010-1	Class A2	6.6	1M BBSW + 1.25%	81.20
15-Dec-10	21-Dec-10	Wide Bay Australia	WB Trust 2010-1	Class AB	6.2	1M BBSW + 2.00%	23.00
17-Mar-11	24-Mar-11	Members' Equity Bank	SMHL Securitisation Fund 2011-1^				0.00
07-Apr-11	14-Apr-11	Community CPS	Barton Series 2011-1 Trust	Class A2	6.5	1M BBSW + 1.25%	30.90
08-Apr-11	13-Apr-11	Liberty Financial	Liberty Prime Series 2011-1	Class A2	4.0	1M BBSW + 1.30%	50.75
15-Apr-11	20-Apr-11	Macquarie Bank	PUMA Masterfund P-17	Class A2	5.6	1M BBSW + 1.15%	157.50
13-May-11	19-May-11	RESIMAC	RESIMAC Premier Series 2011-1	Class A	2.9	1M BBSW + 1.25%	170.00
13-May-11	19-May-11	RESIMAC	RESIMAC Premier Series 2011-1	Class AB	2.4	1M BBSW + 1.75%	22.00
20-May-11	27-May-11	AMP Bank	Progress 2011-1 Trust	Class A2	5.8	1M BBSW + 1.15%	138.00
10-Jun-11	17-Jun-11	ING Bank (Australia)	IDOL Trust Series 2011-1	Class A1	3.6	1M BBSW + 1.10%	206.00
							13372.18

*Weighted average life.

^The AOFM final allocation was zero.

Australian Office Of Financial Management – Objectives

The Australian Government decided to invest in Australian RMBS to support competition in Australia's mortgage market:

- On 26 September 2008 the Treasurer announced that the AOFM would purchase RMBS to support competition in Australia's mortgage markets, with up to $8 billion available for investment.
- On 11 October 2009 the Treasurer announced an extension of the Program, with the AOFM having authority to purchase up to a further $8 billion of RMBS, depending on market conditions.
- To date, the AOFM has invested $12.7 billion in 45 RMBS issues.
- These investments have assisted 19 lenders in raising over $29 billion in funding.
- **The RMBS issuance supported by the Program has financed mortgages over more than 150,000 residential properties across Australia.**
- On 5 April 2011 the Treasurer issued a Direction for the AOFM to invest up to an additional $4 billion in Australian RMBS, including securities by issuers that were not Authorised Deposit-taking Institutions (non-ADIs).
- This is together with remaining capacity from the current program of about $3.5 billion.
- The allocation to the non-ADI sector was made in conjunction with the Government's decision to guarantee the deposits and wholesale funding of ADIs.
- Investments will continue with the aims of supporting competition in residential mortgage lending and lending to small business.
- The Direction also provides clarity regarding the eligibility of issuers operating independently of the four major Australian Banks.
- The Direction further confirms the Program's temporary nature through an additional objective of encouraging a transition towards a sustainable securitisation market that is not reliant on Government financial support.

Achieving the objective

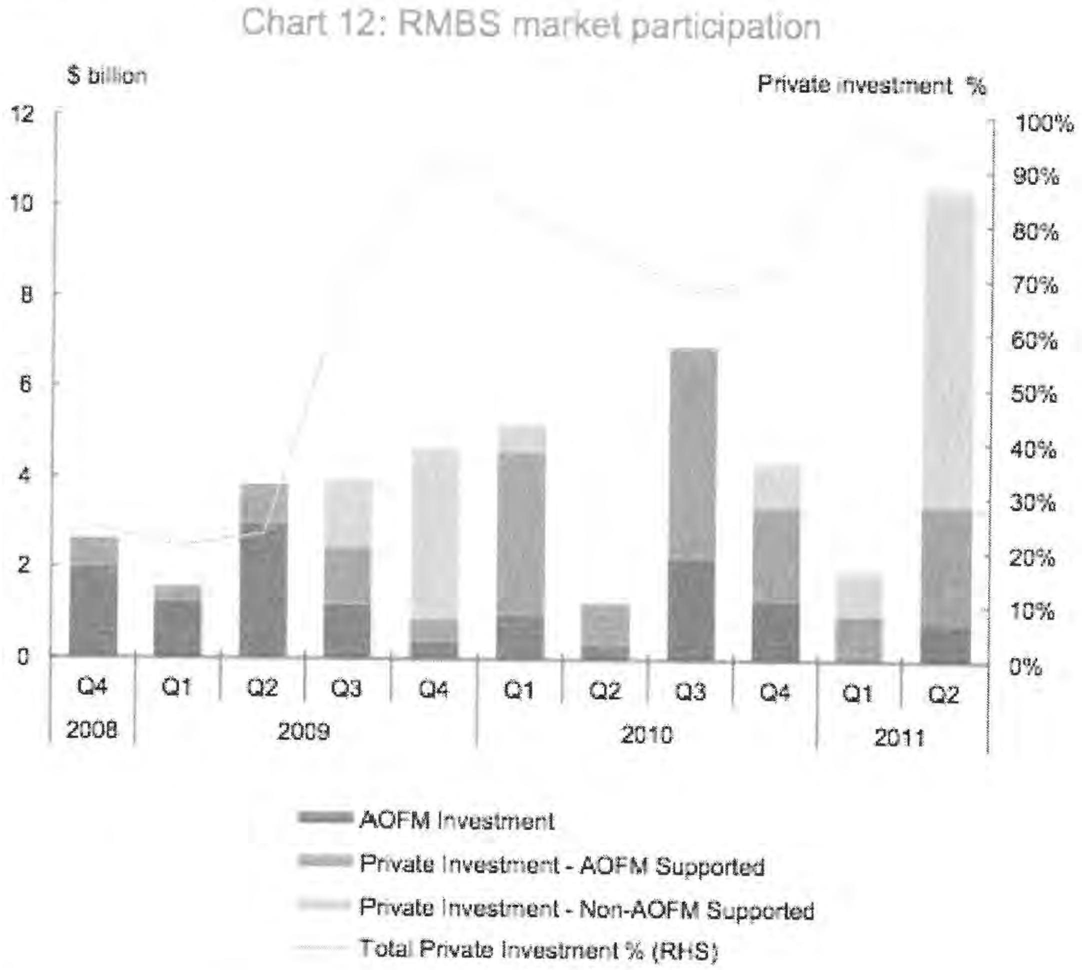
In 2010-11, the AOFM agreed to support 21 RMBS transactions from 14 issuers, investing just under $4.35 billion.

- Since inception of the program the AOFM has invested around $13.37 billion across 49 transactions from 19 issuers.
- AOFM invests via the two investment channels, the serial (or 'pipeline') approach and the reverse enquiry channel, the latter is now the only investment channel used by AOFM
- 2010-11 brought an overall increase in the level of private sector participation in primary issuance and saw the return of three of the largest Australian banks to the RMBS market, as well as the completion of a number of other transactions without the support of the AOFM.
- Table below shows the participation of AOFM and other investors in RMBS issues since the inception of the program.
- Participation from other investors averaged 23 per cent from inception until the end of June 2009
- Throughout 2009-10 and 2010-11 it averaged over 81 per cent.
- In the first six months of calendar year 2011, this proportion rose to around 93 per

cent of total market activity.

- The volume of transactions supported by the AOFM rose to over $14.7 billion in 2010-11 from around $9.1 billion the year before.
- There was also an increase in the volume of transactions that were *not* supported by the AOFM to just under $9 billion from $5.9 billion.
- This brings total public RMBS activity to $23.7 billion in 2010-11, from around $15.1 billion the year before.
- Notably, in the first half of calendar year 2011 there was significant issuance from larger Australian banks and their subsidiaries, as pricing levels moved into line with other sources of funding.
- As a result of these developments, the volume of Australian RMBS outstanding stabilised during 2010-11 at around $80 billion.
- The share of housing credit funded by securitisation also showed signs of levelling out during 2010-11 at just below 10 per cent, according to the June 2011 RBA Bulletin.
- During 2010-11 investor demand returned for RMBS with longer weighted average lives of up to three years.

Table: RMBS Market Participation:



Outcome and performance

- By 30 June 2009, the AOFM had completed 13 RMBS transactions, totalling $6.203 billion, comprising $2.75 billion in six transactions sponsored by five ADIs and $3.453 billion invested in seven transactions sponsored by four non-ADIs.
- Including investments from other parties, the total volume of RMBS that was able to

be issued over this period as part of the program was $8.042 billion. This represented approximately 6.6 per cent of residential mortgages originated in Australia over the period November 2008 to June 2009.

- Interest accrued in 2008-09 was $89 million, which represented an annualised return of 4.80 per cent. The securities purchased in 2008-09 were all floating-rate notes, paying a weighted average margin of around 1.3 per cent per annum over the one month bank bill rate.
- The average credit margin of around 1.3 per cent per annum on the RMBS portfolio is above the AOFM's cost of short-term funding, which has historically been below the bank bill rate.
- This average margin is narrower than margins currently available in the secondary market, and the RMBS held by the AOFM showed an unrealised mark-to-market loss of $136 million in 2008-09.
- The market value of the AOFM's RMBS is determined by an independent service provider. The difference corresponds to a margin of about 80 basis points across the RMBS portfolio.
- This remeasurement effect can be considered to be the opportunity cost associated with purchasing these assets at prices that promote competition in housing lending, rather than at secondary market prices.
- If the RMBS investments had been priced at yields 80 basis points wider, they would not have provided a viable source of funding for housing.
- Details of RMBS investments at 30 June 2009 show a total of $6.203 billion had been invested and had generated capital repayments of $179 million.
- The return of demand for longer maturities has resulted in new transaction structures shifting away from the style supported by the AOFM throughout much of 2010, which sought to attract bank balance sheet demand for shorter life tranches, towards more traditional structures.
- In the first half of 2011, the AOFM was asked to purchase some relatively small longer dated tranches, so as to facilitate the creation of RMBS securities with a weighted average life of around three years, otherwise falling prepayment rates would have meant a weighted average life of closer to four years, ruling out some investor appetite in the process.
- The AOFM also supported a number of structures designed to attract new investors and previous RMBS investors who have been disengaged since the global financial crisis. These structures have enabled issuers to tap new sources of domestic and overseas demand.
- The funds raised by the RMBS issues supported by the AOFM have provided an important component of total lending for housing and small business since the inception of the program.
- Investments made under the program also provide reasonable financial returns. Interest income in 2010-11 was $607 million, which represented an annualised return of 6.07 per cent on the average portfolio book value of $10.005 billion.
- All the securities purchased under the program have been floating-rate notes, paying a weighted average margin of just under 130 basis points over the one month bank bill rate as at 30 June 2011. In addition, capital repayments of $2.5 billion have been received.11
- The RMBS securities that the AOFM holds are valued in its accounts using indicative margins for secondary market trading as estimated by an independent valuation service provider.

- As secondary market margins have typically been higher than the margins set on issuance, the estimated market value of these securities has been less than their accrual book value.
- Despite continued pricing improvements through the narrowing of spreads over the course of 2010-11, the RMBS portfolio had an unrealised loss of $80.8 million (or 0.81 per cent of the portfolio book value) as at 30 June 2011
- Losses or gains in the mark-to-market value of the portfolio change with prevailing conditions and therefore vary at any particular point in time. They are not 'realised' losses or gains

Reserve Bank of Australia

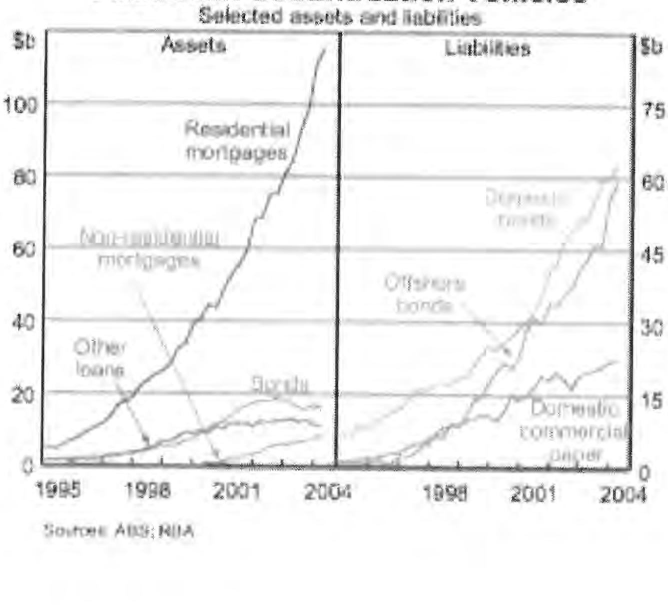
ABN: 50 008 559 486 Page 48
http://www.rba.gov.au/publications/fsr/2004/sep/pdf/0904-1.pdf

Introduction:

- During the last 10 years, the outstanding assets and liabilities of Australian securitisation vehicles have increased from around $10billion in March 1995 to $160billion in June 2004 (Graph 1).
- In addition, the range of assets that has been securitised has broadened.
- Current outstandings comprise $63 billion of domestic bonds and $59 billion of offshore bonds.
- In addition, there is $22 billion of asset-backed commercial paper outstanding.
- Since 2000, more than half of the bonds issued domestically by Australian entities have been asset-backed bonds, while over a quarter of offshore issuance has been of asset-backed bonds.
- The rapid growth in the asset-backed securities market in the past decade has been driven by securitisations of residential mortgages. Securitised residential mortgages have increased from $5 billion to $116 billion and currently account for 70 per cent of the assets of Australian securitisation vehicles.

Table: Australian Securitisation Vehicles:

Graph 1
Australian Securitisation Vehicles
Selected assets and liabilities



Sources: ABS; RBA

Issuers of RMBS:

- The rapid growth in housing finance in Australia in recent years cannot fully explain the growth in residential mortgage securitisations.
- Over the past decade, the stock of securitised mortgages has grown much more quickly than overall housing finance.
- As a result, securitised mortgages now account for one fifth of outstanding housing finance, compared with less than 5 per cent in 1995.
- The growth partly reflects the changing composition of the mortgage market: specialist mortgage originators – who securitise all of their loans – have more than doubled their share of housing lending since 1995.
- Since 2000, mortgage originators have issued $85 billion of RMBS and account for half of RMBS outstanding
- Securitisations have also become a more attractive financing option for traditional mortgage lenders as the deal costs associated with securitisations have fallen.
- Since the start of 2000, regional banks, and credit unions and building societies (CUBS) have securitised about one quarter of their gross housing lending, issuing a total of $47 billion of RMBS.
- The four major banks have funded a smaller proportion (less than 10 per cent) of their new housing loans through RMBS as they have cheaper ways of funding loans on their balance sheets.
- Despite having a share of more than half of the mortgage market, the major banks have accounted for only around 15 per cent ($23 billion) of RMBS issuance since 2000.
- Banks and other deposit-taking financial institutions use securitisations for various reasons.
- The process of selling the loans to a third party, rather than retaining them on their balance sheets, enables them to:
    - manage their credit risk while continuing to maintain a relationship with the borrower;
    - free up regulatory capital so that it can be used more productively;
    - and diversify their funding sources, enabling them to raise funds to finance new lending.

Table: Issuers of RMBS:

Graph 2

Issuance of RMBS by Type of Issuer

2000-2004

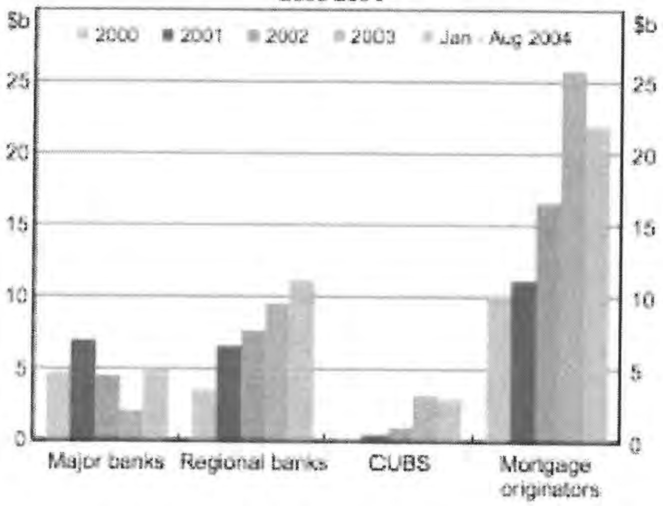


Table 1: Australian Entities' RMBS Issuance

2000-August 2004, A$ billion

	Domestic	Offshore	Total
Major banks	4	20	23
Regional banks	19	20	39
Credit unions and building societies	7	1	8
Mortgage originators	36	49	85
Total	66	90	155
Average issue size	0.4	1.4	0.7
Average spread (basis points)[(a)]	33	28	30

(a) Spreads are weighted averages of spreads above bank bill rates for the senior tranches of prime RMBS. Offshore spreads include the cost of hedging into Australian dollars.

Source: RBA

Credit Quality of RMBS and Underlying Mortgages

Page 50 http://www.rba.gov.au/publications/fsr/2004/sep/pdf/0904-1.pdf

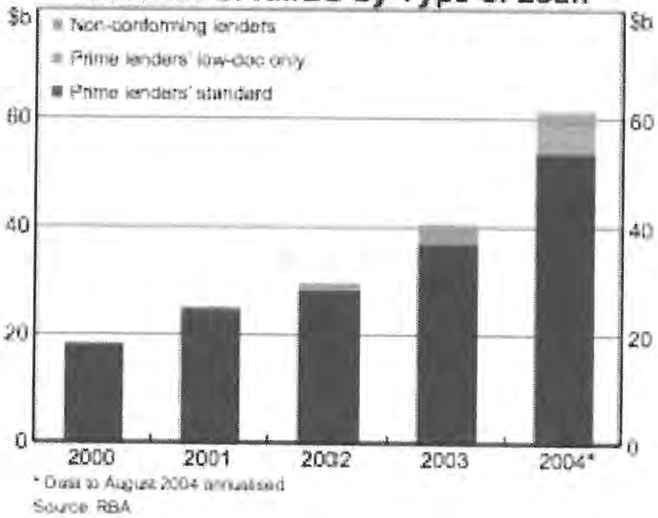
- Prime RMBS account for most of the RMBS issuance by Australian entities, with $145 billion having been issued since 2000.
- A typical prime residential mortgage would be one with a loan-to-valuation ratio of less than 80 per cent, to a borrower with a sound credit history and a full set of documentation.
- However, within the pool of loans backing a prime RMBS there can be substantial variation between individual loans in regard to:
  - loan size;
  - the amount of time that has elapsed since the loan was originated (older loans tend to have lower probabilities of default than more recently originated loans);
  - loan-to-valuation ratio; the amount of documentation provided;
  - and borrower demographics.
- Prime RMBS mortgage pools will often contain some low-documentation ('low-doc') loans

- They are perceived to be more risky than 'full-doc' loans and so are generally required to have a lower loan-to-valuation ratio.
- Partial data since 2003 suggest that, on average, about 10 per cent of the loans in a standard prime RMBS mortgage pool are low-doc loans, however there has been a trend towards issuing prime RMBS backed by mortgage pools comprising solely low-doc loans.
- It may reflect a desire to identify and manage more proactively the credit risk associated with low-doc loans.
- Non-conforming RMBS are backed by a pool of higher risk loans, for example those to borrowers with a poor credit history or those with a high loan-to-valuation ratio (typically over 90 per cent). They tend also to contain a high proportion of low-doc loans.
- Non-conforming RMBS account for a relatively small proportion of Australian RMBS issuance. However, their share of issuance is growing, with $5 billion of issuance occurring in the past two years

Table: Issuance of RMBS by Type of Loan:

Graph 3

Issuance of RMBS by Type of Loan



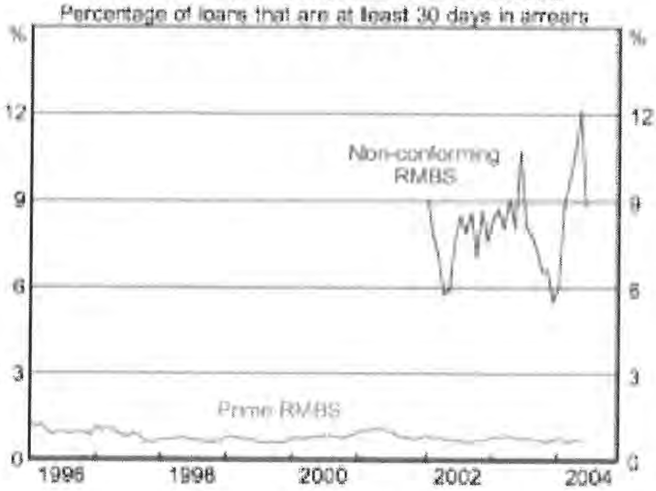
- The mortgage pools backing both prime and non-conforming RMBS will usually contain a balance of investor and owner-occupier mortgages and to date, holders of RMBS have appeared not to distinguish between investor and owner-occupied mortgages.
- Both prime and non-conforming RMBS may also contain loans whose primary purpose is not the purchase or refinancing of a loan on a residential property.
- For example, some refinanced loans include a component that may be used for home renovation, consumption or debt consolidation. Some of the loans in non-conforming RMBS are loans to small businesses that are secured against residential properties.
- Prime RMBS usually have lenders' mortgage insurance, either on the individual loans or on the whole pool of loans up to a certain maximum loss.
- Taken together, the lenders' mortgage insurance, the large number of loans within the portfolios, the property collateral backing the loans, and the low historical arrears on Australian prime residential mortgages mean that prime RMBS are perceived to have a very low probability of default

Table: Loan Arrears on Domestic RMBS:

Graph 4

Loan Arrears on Domestic RMBS

Percentage of loans that are at least 30 days in arrears



- The proportion of non-conforming loans that are 30 days or more in arrears has been noticeably higher and more volatile than that of prime RMBS, ranging between 6 and 12 per cent compared with less than 1 per cent for prime RMBS.
- Cumulative loan losses on mortgages backing prime and non-conforming RMBS have, to date, been small. There have been less than $10 million of losses on currently outstanding RMBS, $71/2 million of which have been on prime loans.
- Most of the losses on prime loans have been borne by lenders' mortgage insurers, while all other losses have been covered by the originator or the excess between the interest rate paid on the mortgages and that payable on the securities.
- As a result, RMBS investors have not suffered any losses

The Structure of RMBS

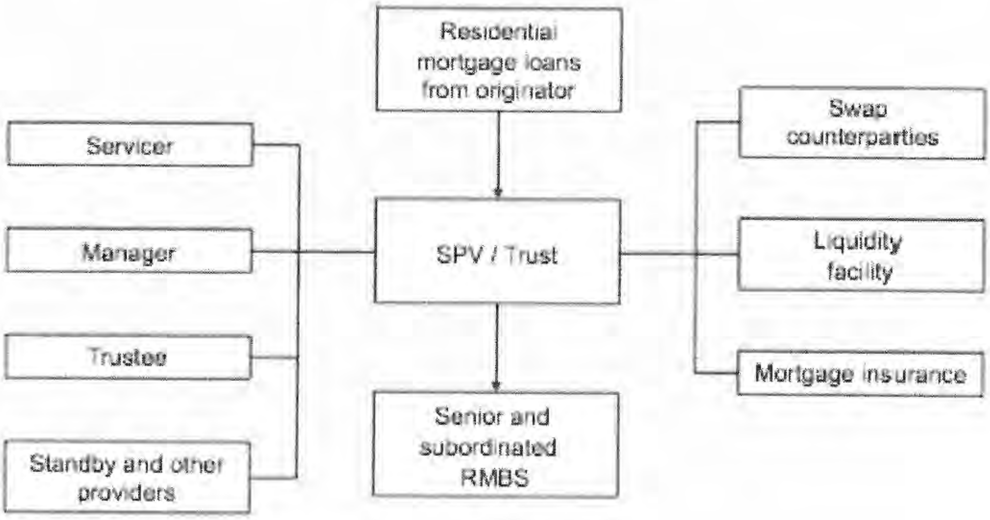
Page 54 http://www.rba.gov.au/publications/fsr/2004/sep/pdf/0904-1.pdf

- The basic process for securitising a pool of assets is as follows (Figure 1). The loan originator sells a portfolio of loans to a special purpose vehicle (SPV).
- The SPV raises the funds to purchase these loans by issuing debt securities (bonds or commercial paper) to investors.
- The cash flow from the loans is used to meet the principal and interest repayments on the securities.
- The loans can be financed initially on or off the originator's balance sheet. Banks and other deposit-taking institutions generally opt for the former and periodically sell a pool of loans to an SPV to be securitised. Mortgage originators tend to do the latter, finding interim funding for the loans from financial institutions or from commercial paper issued by an SPV.
- In most cases, borrowers will not be aware that their loans have been securitised because the originator will continue to service the loans following their securitisation (collecting loan repayments, providing customer service and enforcing delinquent loans). The cash flow from the loan repayments is passed from the originator to the SPV and is used to meet the debt-servicing obligations (both interest and principal) on the bonds and any other on-going costs such as trustee and management fees.
- The sale of the assets from the originator to the SPV is structured so that, in the event

of a default by the originator, the assets should be protected from any claims from creditors of the originator. Likewise, if the SPV defaults on its obligations, the RMBS investor would not have recourse to the originator.

- Second, almost all RMBS benefit from some form of credit enhancement, which is used to raise the credit rating of some or all of the securities above that of the underlying loans.
- The most common form of enhancement comes from splitting the asset-backed security into senior and subordinated tranches. The subordinated securities provide protection for the senior tranche by absorbing the first round of defaults in the pool of assets.
- So long as the value of losses does not exceed the combined amount of the subordinated tranche and any external credit enhancement, the senior securities will be repaid in full.
- Third, the principal of the RMBS is amortised over the life of the security rather than being repaid as a bullet payment when the security matures, reflecting the payment profile of the underlying loans.
- If early repayments of principal are received, these are generally paid through to investors rather than being held with the SPV.
- The amortising principal and ability to repay the loan early means that the average life of an RMBS is substantially shorter than its final legal maturity, which is usually set to occur after the longest dated loan in the underlying portfolio is due to be repaid in full, and is typically around 30 years.
- *Other internal credit enhancement techniques include:*
    - *over-collateralisation, where the face value of the loans is higher than the value of the securities they back;*
    - *reserve funds created by or equity tranches held by the issuer;*
    - *and the excess spread (yield differential) between the interest rate received from the underlying loans and that paid on the securities.*
- To ensure that the RMBS can be redeemed before it becomes uneconomic for the SPV to service the loans and to protect investors from being left with a small, illiquid rump of stock once the bulk of loans have been repaid, most RMBS include an option for the originator to buy back the loans and redeem the RMBS after a certain date or when the aggregate principal outstanding on the mortgage pool falls below a stated threshold (say 10 per cent) of its original face value.
- The option also facilitates the return of any profits from the SPV to the mortgage originator.
- If the option is not called, a higher interest rate may become payable on the securities. The expected life at issue of most RMBS is typically two to five years.

Table : The Structure of RMBS



Securitisation Report: University of NSW

http://knowledge.asb.unsw.edu.au/article.cfm?articleid=1355

- By 2007, RMBS accounted for more than 20% of new housing loans in Australia.
- The practice came to an abrupt end when aggressive lending by US mortgage companies created the "toxic" US sub-prime loans that triggered a meltdown of the global financial system.
  Since then, these securitised products have received a bad rap.
- Some US commentators have suggested RMBS should be banned.
- The big kicker for the Australian RMBS industry before the crisis was its attractiveness to international buyers.
- Two-thirds of demand was soaked up by a large pool of highly leveraged, structured investment vehicles (SIVS) in London and New York.
- "If there was a problem with securitisation, it was in the execution," says Christopher Adam, a finance professor at the Australian School of Business. "There was failure in the risk-rating process and failure to administer newer products. Less informed investors were persuaded they could obtain good returns and little risk because the process is so opaque."
- Investors in a securitised pool do not have a clear view of the line of cash flow coming off the mortgage payments into the securitiser's portfolio.
- Some investors who were achieving a good return may not have understood they were taking a higher risk by investing in assets that were effectively lower than investment grade, but that were rated above that.
- An even bigger issue concerns the pricing of risk: RMBS pools were usually rated on default risk when they should have been valued on market risk
- In Australia, the value of the underlying asset did not decline and defaults were low, but in other regions the story was different.
- The liquidity crisis forced debt-stricken Europeans to dump bonds on the market, causing the price of bonds to plummet. The reasons for securities markets freezing up had "more to do with the market machinations rather than the underlying credit associated with many of the individual securities in Australia"
- While some claim the market is functioning properly, it could be argued that any market that's reliant on government participation is not

- RMBS investors are separated from the assets. Investors in a mortgage-backed security have exposure to a specific and definite pool of mortgages. And, if they invest in a senior unsecured bonds issue of a bank, they are still exposed to all commercial lending.
- RMBS investors also have first-ranking security over securitised assets that no one else can touch. If the underlying seller goes bust, these securities are structured so the investors still have access to the mortgages
- Homeowners will re-finance if they want to keep their homes.
- The securities will be repaid based on the underlying cash flows as long as the home owners continue to pay.
- The holder of the securitised paper will be paid their coupon and principle on a progressive basis.

Securitisation and Bank Liquidity:

There are at least four dimensions relating to liquidity:

- Overall mortgage marketability and liquidity are improved through securitisation
    - e.g., Black et al., 1981; Gorton and, Pennacchi, 1995; Kothari, 2006);
- The process of securitisation changes the nature of assets
    - e.g., Schwarcz, 1994; Hill, 1997), transforming illiquid assets (e.g., mortgages) into marketable securities;
- Security designs with pooling and tranching enhance asset liquidity
    - e.g., DeMarzo, 2005), reallocating cash flows, risks and information;
- Banks' liquidity positions are strengthened
    - e.g. Berger and Udell, 1993; Thomas and Wang, 2003).

RMBS Disclosure & Reporting Standards

Australian Securitisation Forum Standards
http://www.securitisation.com.au/Default.aspx?PageID=6302429&A=SearchResult&SearchID=5857660&ObjectID=6302429&ObjectType=1

Key Legal Issues

Page 160 http://www.austlii.edu.au/au/journals/MonashULawRw/2007/5.pdf

- True Sale: One of the key concerns in RMBS programs, both for law and prudential regulatory purposes, is whether sufficient risk and reward have been transferred from the originating bank to the SPV in order to justify a finding that a 'true sale' of the mortgagee's rights has occurred.
- It will not be if, for example,
    - the originating bank retains influence over the setting of interest rates or the way in which delinquent assets are followed up;
    - the originator retains a right to share in any profits of the SPV,
    - or investors in the RMBSs have any recourse back to the originating bank.
- If a 'true sale' has not been effected, the mortgaged loans unsuccessfully assigned will lose their off-balance sheet status for regulatory and accounting purposes, and

will be re-characterised as normal on-balance sheet secured loans.

- This plainly has significant consequences for, amongst other things, a financial institution's capital adequacy and taxation obligations.
- Ascertaining whether a 'true sale' has occurred is made more difficult by the fact that there is no Australian case on point, and the few cases that have been decided overseas are somewhat inconsistent.

AOFM Investment Facility Dealing Panel

Panel Members as at 7 April 2011
Australia and New Zealand Banking Group
Bank of Scotland PLC Australia Branch
Bank of Tokyo-Mitsubishi UFJ Ltd
Barclays Bank PLC
BA Securities Australia Limited
BNP Paribas
Citibank NA
Citigroup Pty Ltd
Commonwealth Bank of Australia
Credit Suisse
Deutsche Bank AG Sydney Branch
FIIG Securities Limited
HSBC Bank Australia Limited
HVB Australia Pty Ltd
The Hongkong and Shanghai Banking Corporation Limited Australia Branch
ING Bank (Australia) Limited
J.P Morgan Australia Limited
J.P Morgan Chase Bank N.A
Laminar Capital Pty Ltd
Lloyds TSB Bank PLC Australia Branch
Macquarie Bank Limited
Mizuho Corporate Bank Ltd, Sydney Branch
National Australia Bank Limited
Nomura Australia Limited
Royal Bank of Canada S
ociete Generale Australia Branch
Sumitomo Mitsui Banking Corporation Sydney Branch
Suncorp-Metway Ltd
The Royal Bank of Scotland N.V. Australia Branch
The Royal Bank of Scotland PLC Australia Branch
The Toronto-Dominion Bank
UBS A.G. Australia Branch
Westpac Banking Corporation

Purchase of RMBS by AOFM – Update No: 2/2011 8 April 2011
http://www.aofm.gov.au/content/notices/02_2011.asp

AOFM RMBS Portfolio Manager
Hulya Yilmaz

Matters (c), (d) and (e) referred to the Senate Economics References Committee (the Committee) for inquiry and report on recent developments in the banking sector arising out of the impact of the global financial crisis and subsequent events, are:-

(c) the impact on borrowing and lending practices in the banking sector both during and since the global financial crisis;
(d) the need for further consideration of the state of the broader finance and banking sector; and
(e) any other relevant matters.

BFCSA note:-

The Government has 'bought' **14 billion dollars worth of RMBS** since the GFC and has committed another 4 billion dollars to further purchases.

Fitch say 8 to 10% of all RMBS are lo doc. Approximately 2 billion then are loans obtained by fraud and the Government is holding tainted securities and profiting by fraud.

A Government cannot, or at least, cannot be seen, to be profiting from the fraud of its constituents and must rectify the situation. The Government must also rectify all of the other loans secured on falsified loan application documents because the Government's regulator, ASIC, has failed to regulate the financial industry as required by the ASIC Act.

ASIC did nothing before the GFC, nothing during the GFC and have refused to do anything since the GFC as their letters to BFCSA state.

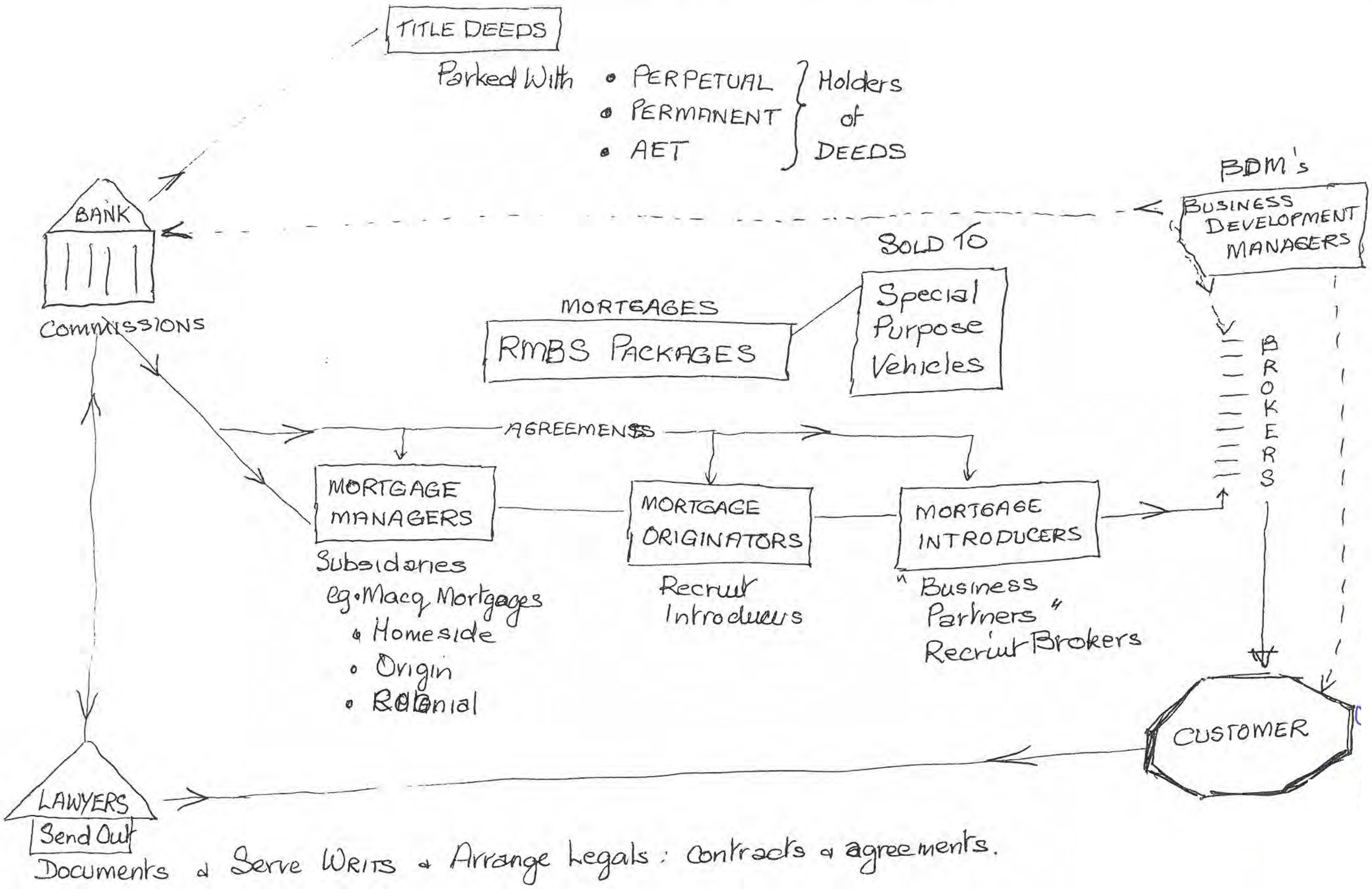
The path to rectification centres on this premise:-

Any lender who approved a loan without verifying the loan application data with the borrower was imprudent, negligent and in many cases, reckless. Indeed, most of the loans made would have been rejected if the lenders had contacted the borrowers and ascertained the borrowers true financial circumstances.

In the case of the 25 Australian Banking Association members, they are also in breach of their contract with the borrower to assess **the borrower's ability to repay** the loan as provided for in Article 25 of the Code of Banking Practice.

No lender, and no holder of loan securities, including the Government, should be allowed to maintain any loan which the lender would not have given had it applied the simplest of lending criteria tools, namely, verifying the loan application details with the borrower.

SIX LINKS in CHAIN



QUESTIONS TO MR MEDCRAFT – ASIC Nov 2011

On behalf of all consumers of banking products and services in Australia, the two key questions we are seeking answers to are these:-

1. Which Bank flagged a hybrid Low Doc Model to all the other lenders so that the product miraculously appeared on every lender's books at the same time?

2. Which Bank designed the six degrees of separation between lender and borrower and ensured the plans were identical?

A relevant sub-question 2 (a): if it wasn't for the Banks intended 'arms length' to claims from down the chain, why was the same arms length, otherwise necessary?

Pensioners and Low Income families, labelled by those banks as "Asset Rich Income Poor" ("ARIP's"), are now dependent upon urgent responses to these two questions in order to avoid being thrown out into the street.

<u>AGAINST LENDING POLICY GUIDELINES:</u> **a selection of quotes from the emails**

Good news – can now do ABN's for a Day

NO GST Registration
NO Asset and liability Statements
No minimum self-employed
No more service calculators (in favour of NO DOCS)
No LMI – paid by the Funder
Up to 105%LVR Up to 90% LVR
Loan limits up to $3 million – up to $5.5 million
Split Loans $1 million ea – Jumbo Loans
No genuine savings required
Credit Assessors had Direct Contact with the brokers
PAYG Low Docs *{How can it be if self employed}*
LOC available
Re-Draw available...unrestricted cash out......
Regulated or Unregulated 95% Regulated and 90%LVR Unregulated
No valuation fees
No statements required
Unlimited debt consolidations
Service Calculator to "make it fit..."
Target Older Persons
Same day approvals

Instructing Brokers: -

Earn 1.4% up front Plus Trails.
As a "valued Business Partner" we invite you to......Sth Africa.....
Tap into debt stress market
Credit Impairment Calculator
Unlimited number of defaults and discharged bankrupts
Switching from Low Doc to No Doc? *"yes but needs to be re-written as we have seen the A&L and Income details."*