



**Exploring SME financing through  
securitisation and mutual guarantee  
consortia: The Italian experience**

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- **Agenda**

**The Italian entrepreneurial structure**

**Measures in support of SMEs**

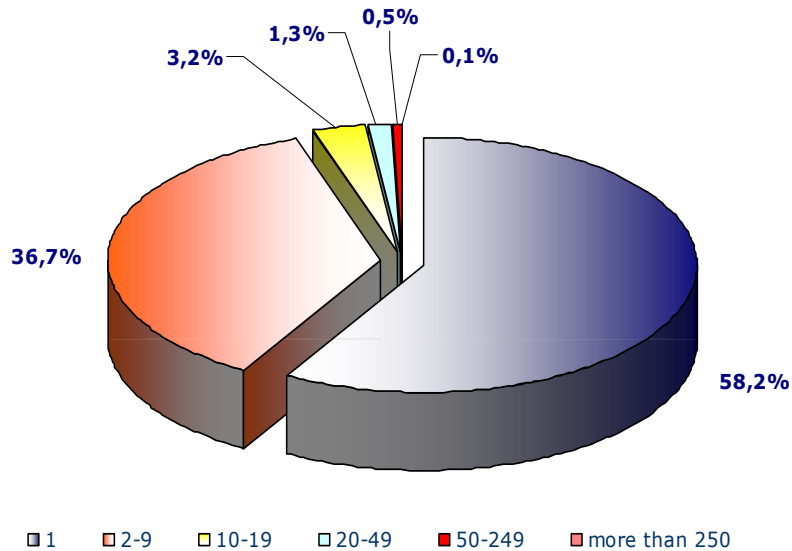
**Credit Risk Mitigation Techniques**

**District bonds**

**Tranched cover schemes**

## ▪ The Italian entrepreneurial structure

By number of employees



almost 95%  
with less than  
10 employees



- Low capital levels
- Closed family ownership
- Poor transparency

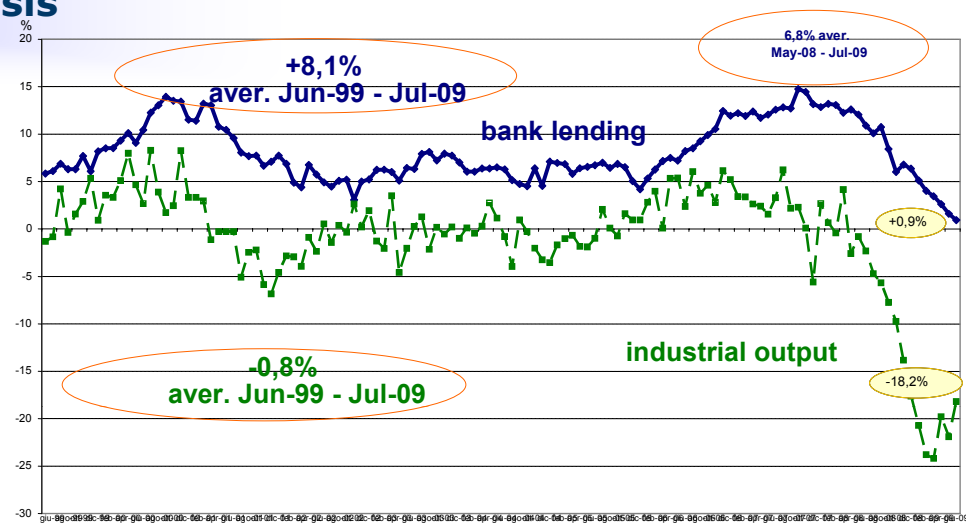


Difficult bank-firm relationship

## ▪ Banks' dilemma during the current crisis

*change in demand*

- To keep supporting SMEs access to credit
- To avoid credit standards deterioration



Source: elaborazioni Centro Studi e Ricerche Abi su dati Banca d'Italia e Istat.

## ▪ The role of credit risk mitigation techniques

- ✓ Reduction in the credit risk arising from bank-SME information asymmetry
- ✓ Credit risk transfer
- ✓ Regulatory capital optimisation

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### ▪ Measures in support of SMEs

✓ Tremonti Bonds

✓ ABI - CDP Agreement

✓ ABI - EIB - Italian Manufacturers' Association Agreement

✓ ABI - SACE Agreement

✓ Common Advice (Government - Banks - Enterprises)

### ▪ Tremonti bonds

#### OBJECTIVE OF THE INTERVENTION:

*“In order to ensure an **adequate flow of financing to the economy** and an adequate **level of capitalisation** to the banking system, the **Ministry for Economy and Finance** is authorised, until **31 December 2009**, ... to **underwrite**, on specific request from the interested banks, **financial instruments** ... eligible for inclusion in regulatory capital and **issued by those Italian banks** whose shares are traded on regulated markets, or by parent companies of Italian banking groups ... ”.*

#### **The subscription is subject to:**

- *“the implementation, by the Bank and by the Ministry, of the protocol ... defined on the basis of a **framework agreement between the Ministry and ABI - Associazione Bancaria Italiana** on the aggregate availability of **credit to be granted in favour of families and small and medium enterprises**, determined by taking into account the economic development needs of the economy, the expected credit demand and the necessity to ensure a **prudent allocation of the credit**”.*
- *“the adoption, by the issuers, of a **code of conduct** which includes, inter alia, provisions governing the remuneration of top management.”*

### ▪ Tremonti bonds (in sum)

- ✓ Very important during the “hot days” of the crisis
- ✓ Announcement effect highly positive for the industry
- ✓ Main problem: timing. Elsewhere, banks are now starting to reimburse the funds obtained by the governments...
- ✓ Cost conditions reflect the tough times when they were designed (October 2008)
- ✓ Since they are not tax deductible, the notional cost of 8,5% rises to around 12.5% (and up to 20-25%)
- ✓ The main road to banks capital strengthening is NOW the market
- ✓ Each bank has its own cost of capital and each bank has the right to choose the most convenient way to re-capitalize

- **ABI-CDP Agreement**

**Date:**  
*May 28, 2009*

**Objective:**  
*To make CDP funding available to banks for the purpose of allowing the granting of loans with a maturity in excess of twelve months in favour of **SMEs operating in Italy.***

**Content:**  
*Within the scope of the new action to bolster the country, CDP makes funding available to **support SMEs**, which have a significant impact on the domestic production environment. The **funds are made available and distributed through the credit system.** Loans to credit institutions have a **maturity of five years**, thus meeting longer term funding needs. The initial interest rate applied by CDP is equal to the six-month Euribor, plus 75-95 b.p., depending on the capitalisation of the banks.*

**Available funds:**  
*8 billion euros*

### ▪ ABI-SACE Agreement

**Date:**

**June 30, 2009**

**Objective:**

**To promote enterprises' access to the credit market, by hedging default risk.**

**Content:**

- a) **SACE Guarantee on bank advances with respect to enterprises' receivables from the Public Administration;**
- b) **SACE Guarantee on bank loans granted to SMEs by using CDP funds.**

**Guarantee:**

**Covers up to 50%, in terms of principal and interest, of the amount of the loan granted to the enterprise.**

### ▪ Common advice

**Date:**  
**August 3, 2009**

**Objective:**  
**To share** the commitments **in favour of those SMEs** that, due to the **crisis**, are facing **temporary financial difficulties**

**Content:**

- **a 12 month suspension** on the **principal amount of mortgage payments**;
- **a 6-12 month suspension** on the **principal amount of lease payments for movable-immovable property**;
- **an extension to 270 days** of the **maturities of short-term credit** granted for liquidity needs, with reference to advances on credits due and payable;
- **contribution to the recapitalisation** of small and medium-sized enterprises through specific loans.

**Available funds:**  
**Euro 30-40 billion** in the next 12 months.

### ▪ Common advice

#### **How it works**

- *The instalments must be **outstanding or overdue** by no more than **180 days** at the application date;*
- *To be eligible, enterprises must be deemed to be "performing" by the bank as of 30 September 2008, and they must not hold "restructured" or "non-performing" positions, or be involved with ongoing enforcement procedures, as of the date of request.*
- *the suspension of the repayment of the principal of the instalments entails the **extension of the amortization schedule for a similar period of time**; the interests accrued on the suspended principal amount are paid on their original maturities;*
- *applications may be submitted **until 30 June 2010**.*

**Number of participating banks:**  
**approximately 500; 32,000 branches (94% of total)**

- **Agenda**

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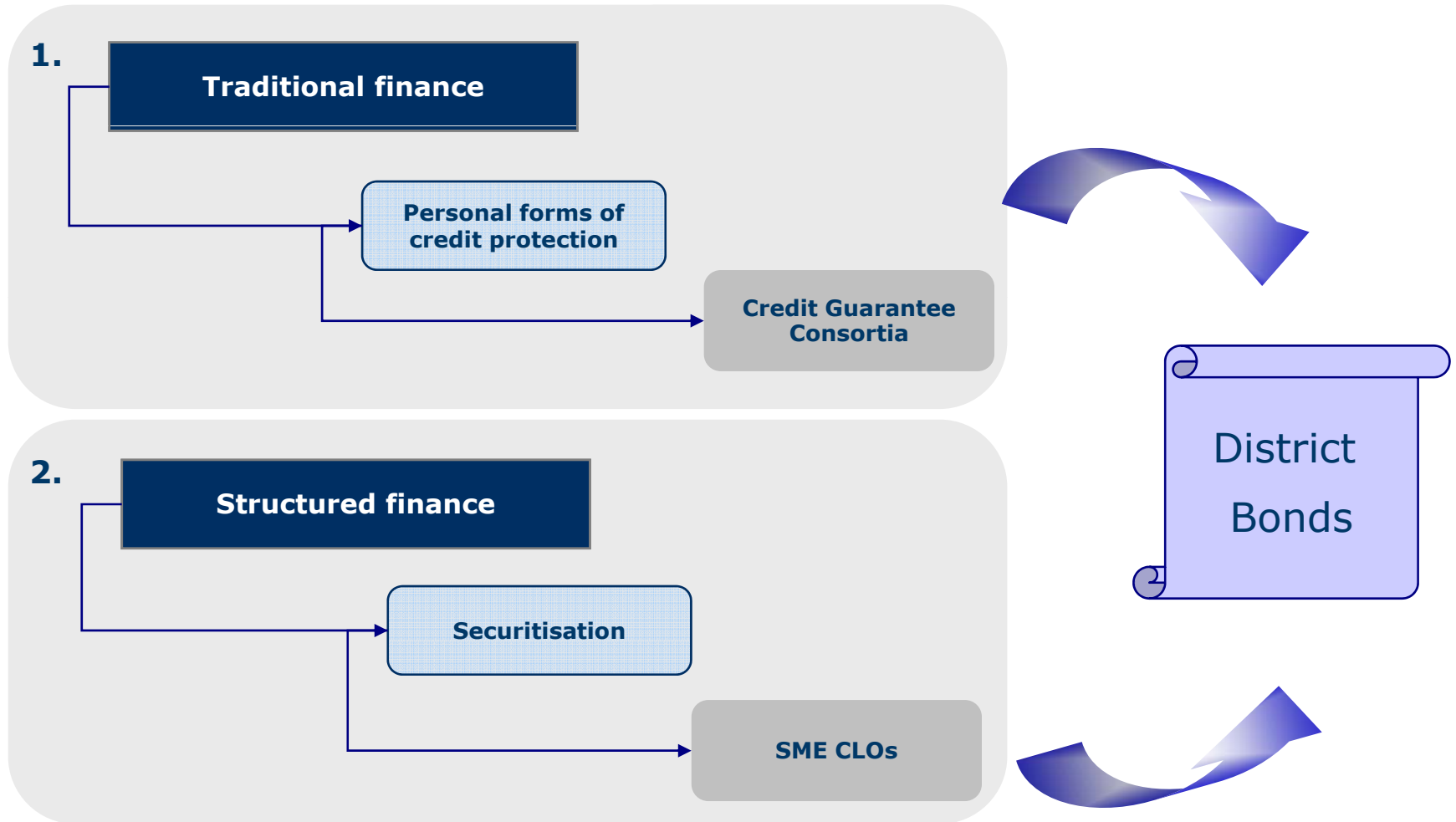
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- 2 main forms of CRM for SMEs



- **Traditional finance: the role of Confidi**

### ▪ The nature of Confidi

Credit guarantee consortia (aka "Confidi") are organisms created to offer an accessory guarantee to the lending bank and therefore to help member firms to have a better access to the credit market.

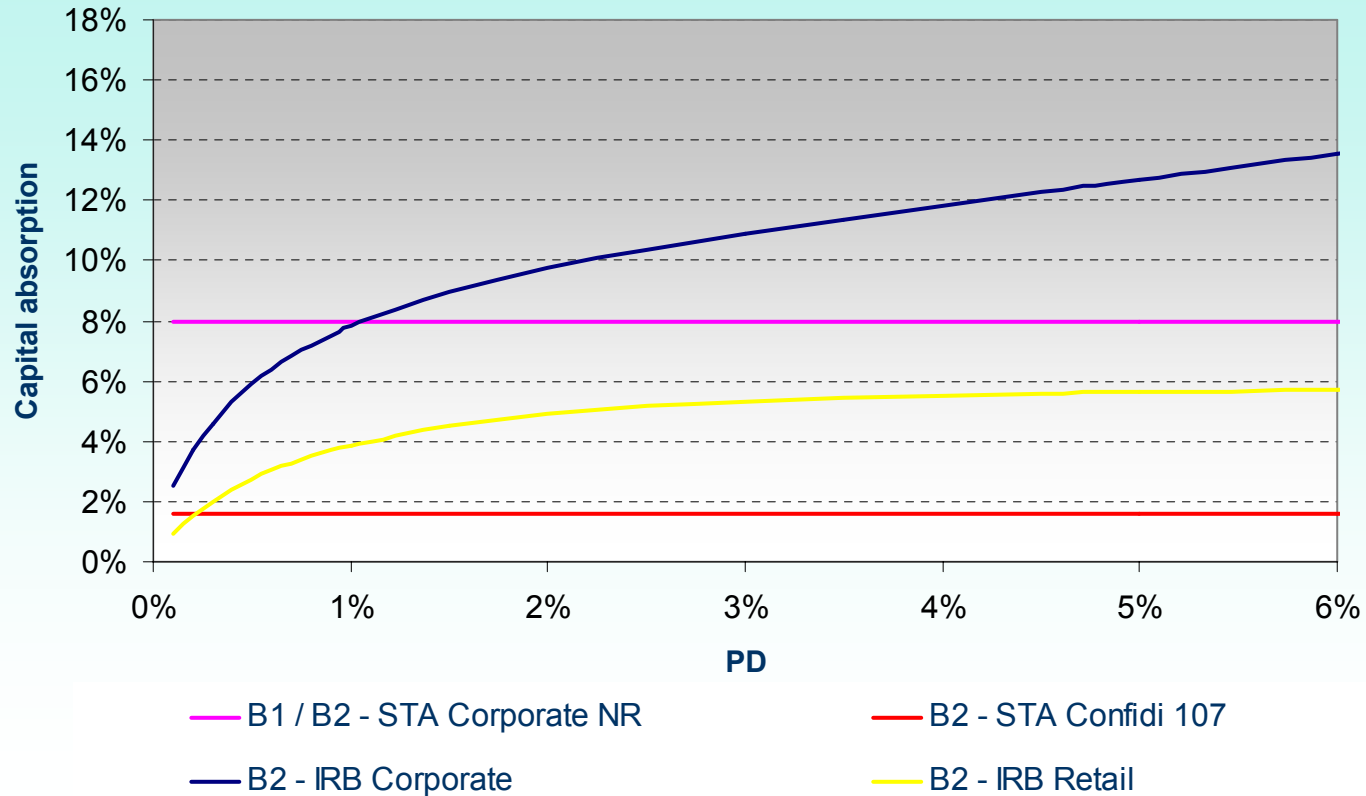
Through the constitution of collective loan guarantee funds with the contributions of member firms and those of the promoting public authorities, Confidi ensure a partial or even total reimbursement of the losses incurred by banks when one of their members defaults.

The economic rationale behind Confidi's existence is:

- i) to help small business firms which individually would be turned down, to obtain bank credit;
- ii) more generally, to help small firms to obtain more credit than they would individually, and at more favourable terms.

**In Italy there are currently 360 Confidi providing guarantees for more than €20 billion**

- The effect of Confidi on banks' capital requirements



- **Structured finance: SME loans securitisation**

- **Obstacles to Italian SME loans securitisation:**

### 1. Internal obstacles:

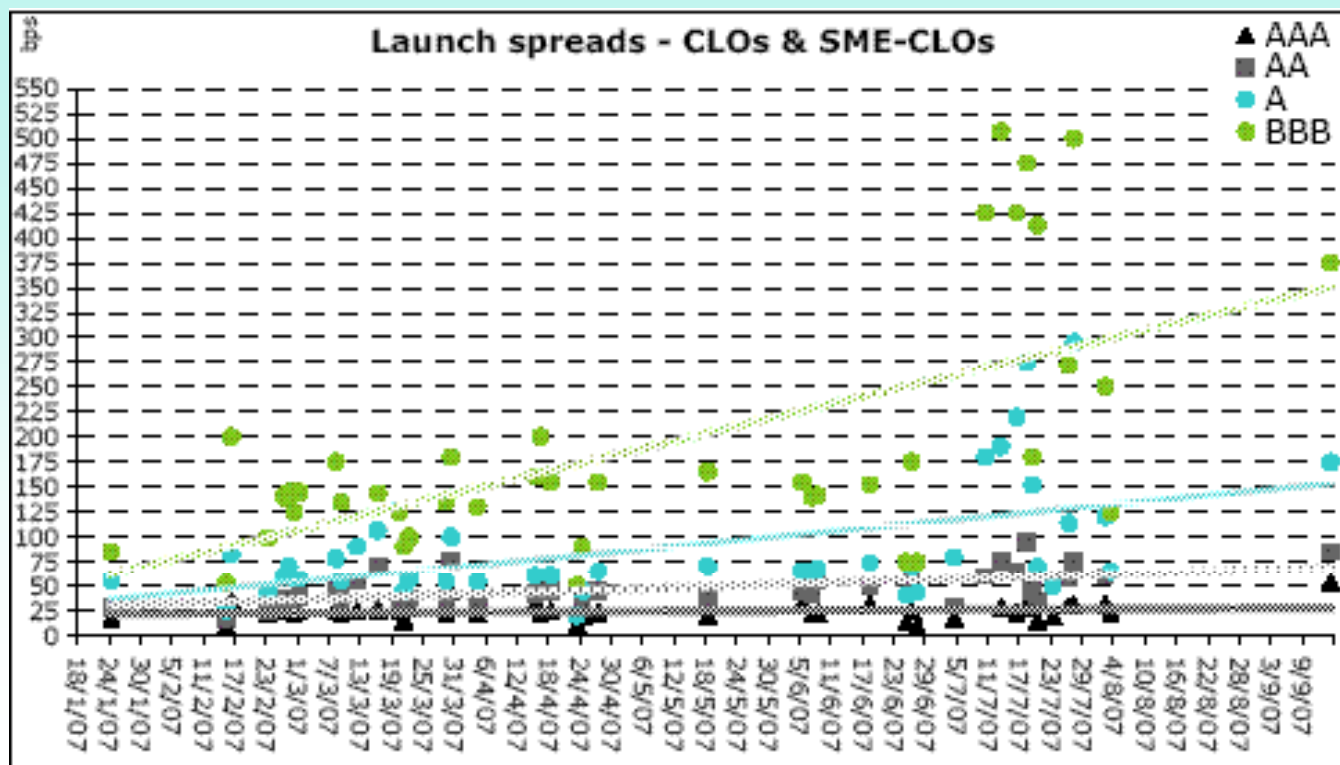
- Lack of long time series data on the default frequency of SMEs;
- Heterogeneity of SME portfolios which differ among one another in terms of size, corporate form, business activity and geographic location;
- Insufficient volumes of long-term loans which hamper a correct estimation of the cash flows pattern of SME portfolios.

### 2. External obstacles:

- High set-up costs;
- Regulatory treatment of junior tranches and low-rated ABS.

- Obstacles to Italian SME loans securitisation:

## 3. The current financial turmoil:



source: DBRS

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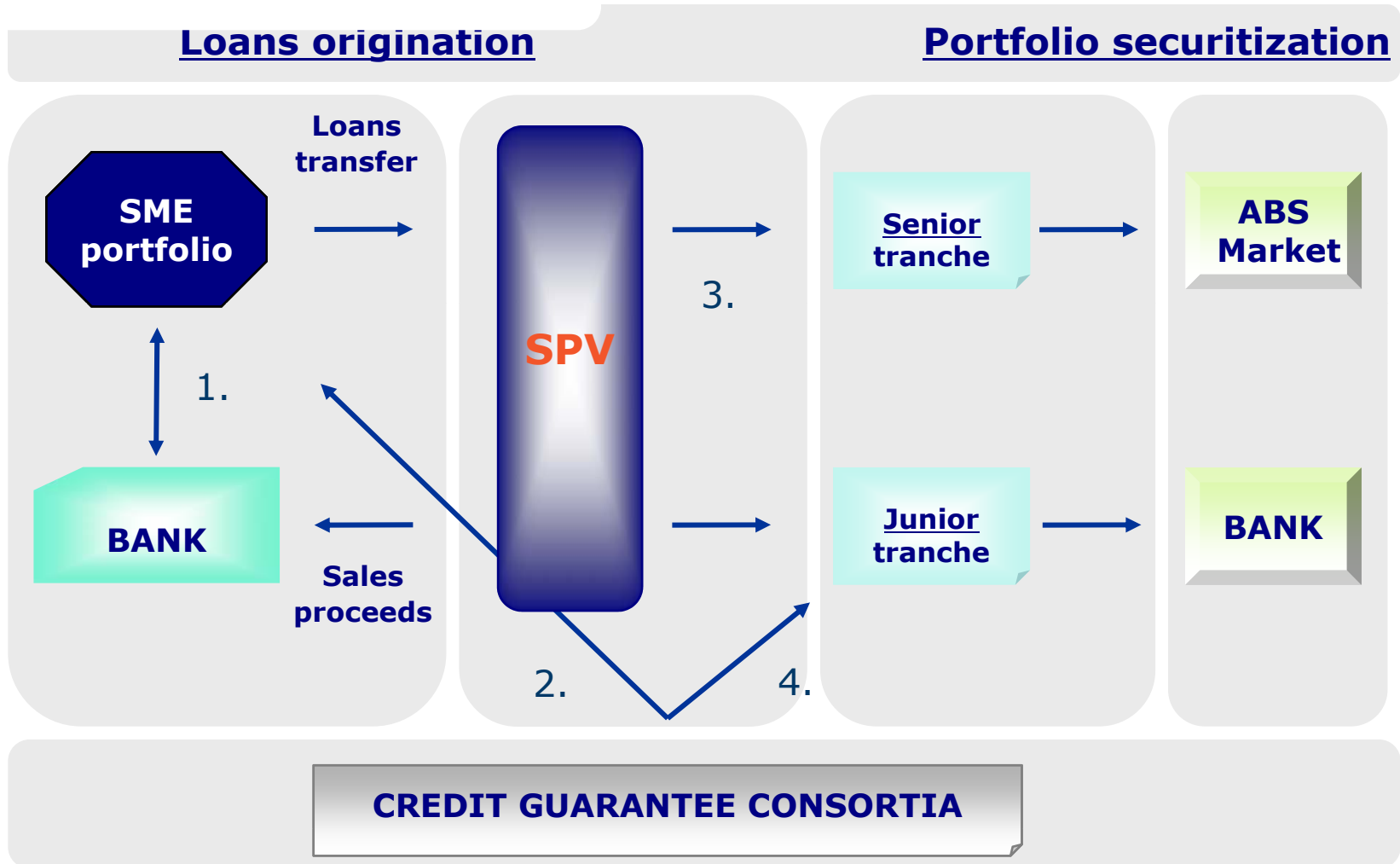
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- The structure of a district bond



### ▪ Benefits for SMEs

- **Access to international capital markets – normally available only to corporate firms – and chance to diversify their funding sources;**
- **Rebalancing of their financial structure towards longer maturities, through a medium-long term funding**
- **Less expensive cost of credit with respect to traditional forms of bank loans, and without the need to provide collateral;**
- **On the bank side, capital relief which will raise the amount of capital available to SME lending.**

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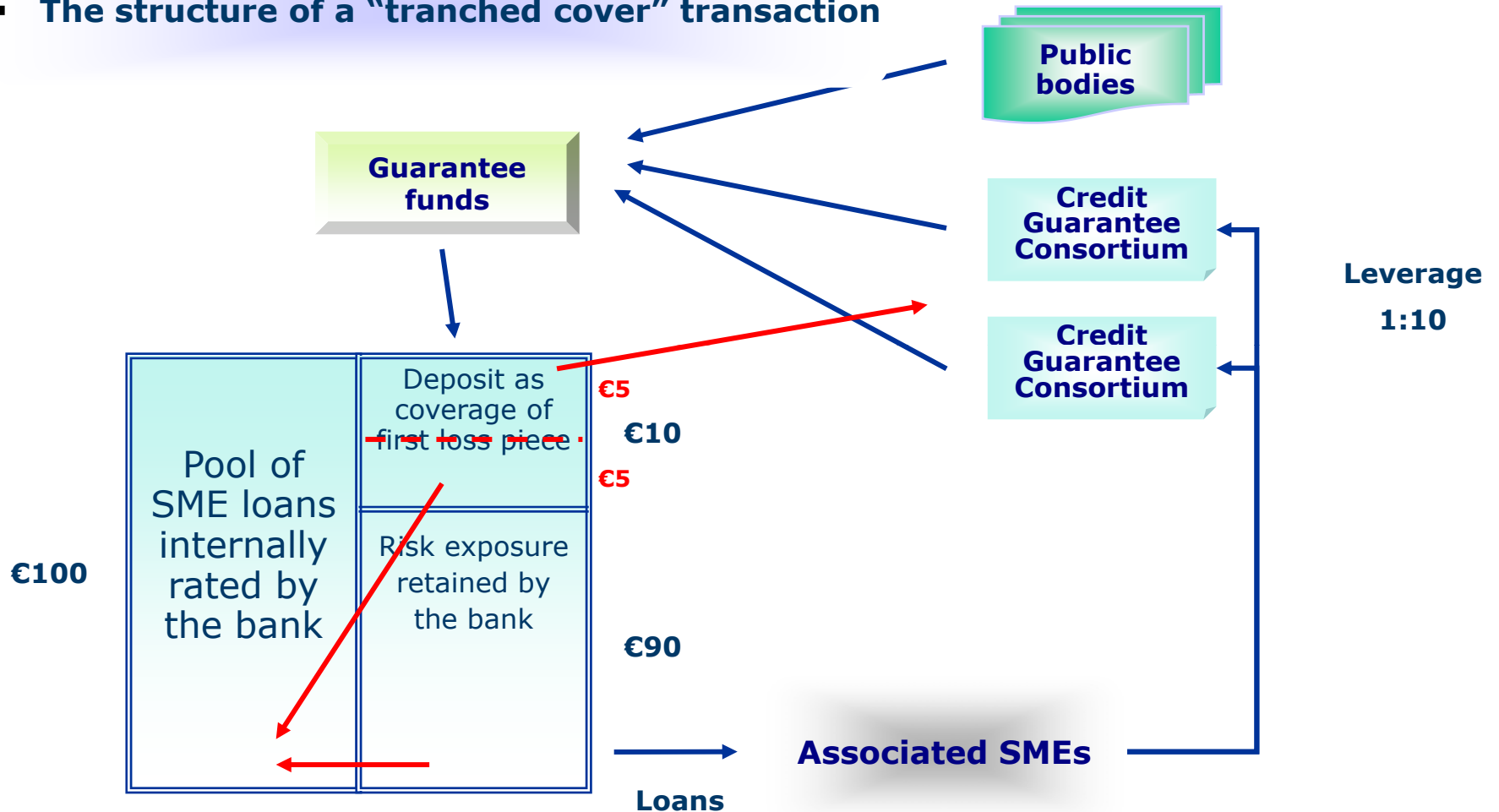
- **Awaiting recovery: “Tranched cover” structures**

Confidi’s monetary fund, acquired by the bank as deposit, works just as the equity piece in a securitisation transaction, i.e. it absorbs the first loss incurred on the SME portfolio, up to an amount equal to the fund itself.

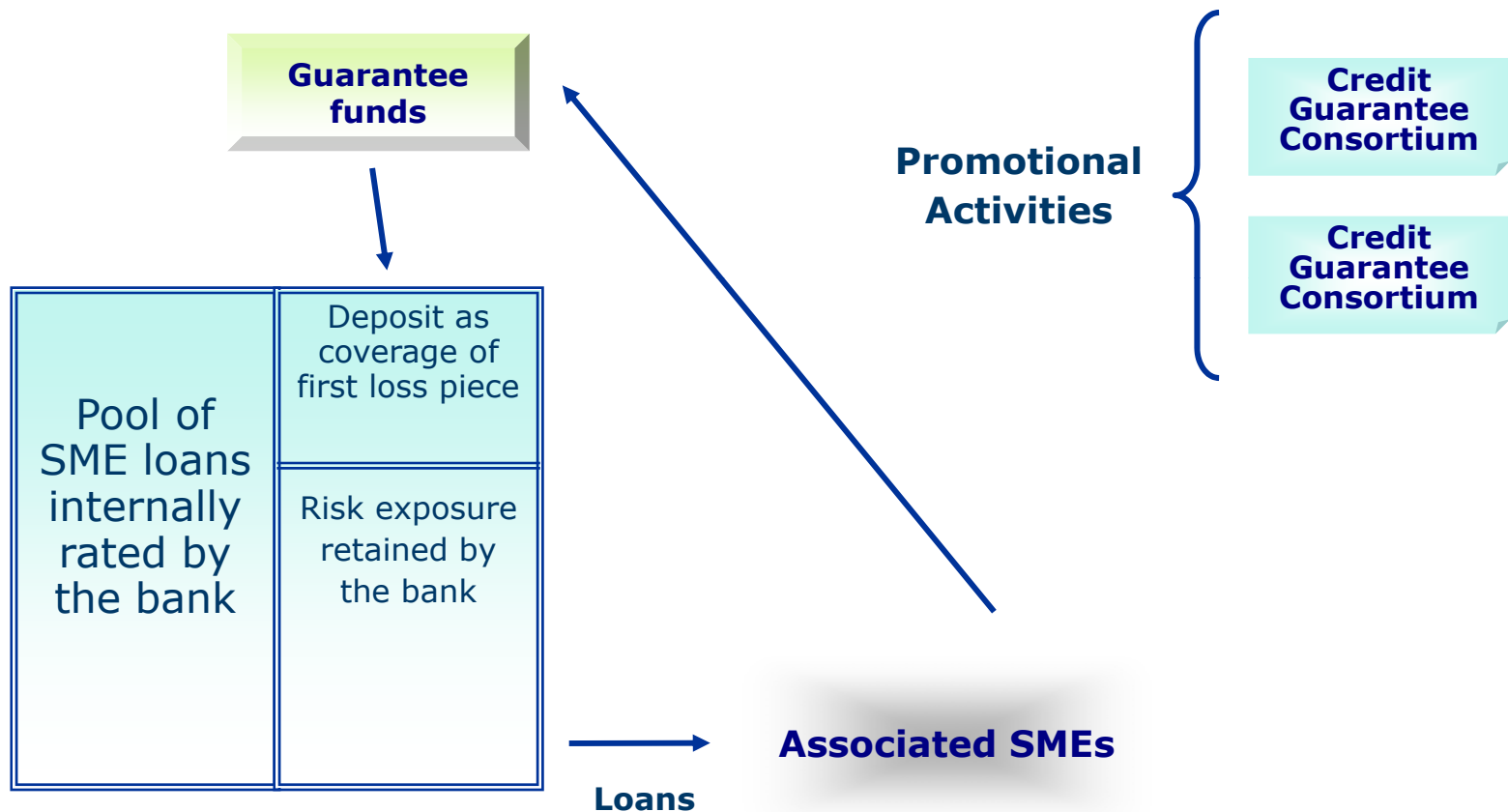
In light of the above, Supervisors allow to apply to such schemes the rules governing securitisation, in order to evaluate the credit risk mitigation effect provided by Confidi’s fund.

This guarantee scheme, different from both a personal and a real form of credit protection, is known in the new Basel 2 terminology as “tranching cover”, that is a transaction which provides a risk segmentation implying different levels of subordination.

- The structure of a "tranching cover" transaction



- The structure of a “tranching cover” transaction



# Thank you!

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