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Student Loan Securitizations: SLABS Popularity Rising

Student loan securitizations are both an established and evolving asset-backed product. Driven by significant increases in advanced-education costs (which have consistently outpaced inflation), and the increasing percentage of students pursuing advanced degrees in all OECD countries, the demand for student loans is expected to continue growing. As the most efficient funding mechanism for these loans, the volume of student loan asset-backed securities (SLABS) has grown in tandem.

According to the College Board, the average annual tuition and fees (excluding room and board) for private and public four-year colleges increased 50.4% and 53.7%, respectively, from the 1983-1984 to the 1993-1994 academic years. It rose another 35.3% and 44.0%, respectively, for the subsequent ten-year period to the 2003-2004 academic year (constant 2004 dollars). With students and their families squeezed by these rising costs, student loans have become the method of choice for financing most undergraduate and graduate degrees. Within the United States, there are roughly three lending sources for students and their families: direct government loans; the Federal Family Education Loan Program (FFELP); and private loans.

By far, the largest loan source is the FFELP. All loans funded through the FFELP are ultimately guaranteed by the U.S. Department of Education (DOE) through reinsurance commitments to eligible loan guarantors. Consequently, the markets consider FFELP loans to be, effectively, U.S. government obligations. The DOE reports that total FFELP loan commitments for the department's 2002-2003 (ending September 30) fiscal year was \$38.9 billion, an 18.7% increase over the previous year's total commitments. A recent College Board publication states that, for the 2003-2004 fiscal year, student loan activity totaled \$66.8 billion, of which 83.1% was through various government-related direct lending and guaranteed loan programs. Of the \$11.3 billion in non-Federal loans, 94.0% of the funding came from the private sector. Led by Sallie Mae, originally chartered as the Student Loan Marketing Association (a U.S. government-sponsored enterprise), and followed by the steady growth of private originator/issuers, the SLABS markets have absorbed most of this increased volume.

Major issuers of SLABS include: First Marblehead Corp., Nelnet, College Loan Corp., Education Funding Capital Trust, Collegiate Funding Services, Education Loan Asset Backed Trust, Brazos Group, and Keycorp. For a broad range of institutional investors, SLABS satisfy target returns for ABS characterized by comparable credit and prepayment risks. Key non-credit risks include origination procedures and post-issuance servicing. Non-compliance with the strict and precise origination/servicing rules can adversely affect the enforceability of collateral guarantees. Consequently, upfront and ongoing originator/servicer due diligence is critical.

Total U.S. SLABS Issuance (billions, year-to-date)

	12/31/2001	12/31/2002	12/31/2003	09/30/2004
Sallie Mae	6,139.3	14,102.8	31,070.8	28,060.9
Other/private	4,911.4	11,769.1	13,502.7	14,408.5
Total	11,050.7	25,871.9	44,573.5	42,469.4

Source: Asset-Backed Alert.