U.S. Structured Finance Newsletter

Volume 4, Issue 49, December 1, 2008

DBRS

Claire Mezzanotte
Managing Director, ABS/RMBS
U.S. Structured Finance,
+1 212 806 3272
cmezzanotte@dbrs.com

Jan Buckler
Senior Vice President,
Research and Modeling
U.S. Structured Finance
+1 212 806 3925
jbuckler@dbrs.com

David Hartung
Senior Vice President, ABS
U.S. Structured Finance
+1 212 806 3269
dhartung@dbrs.com

Quincy Tang
Senior Vice President, RMBS
U.S. Structured Finance
+1 212 806 3256
qtang@dbrs.com

Kathleen Tillwitz
Senior Vice President,
Operational Risk
U.S. Structured Finance
+1 212 806 3265
ktillwitz@dbrs.com

Toronto
DBRS Tower
181 University Avenue
Suite 700
Toronto, ON M5H 3M7
+1 416 593 5577

New York
140 Broadway, 35th Floor
New York, NY 10005
+1 212 806 3277

Chicago
101 North Wacker Drive
Suite 100
Chicago, IL 60606
+1 312 332 3429

TREASURY PROVIDES FUNDS TO CONSUMER ABS LENDING FACILITY

On November 25, 2008, the U.S. Treasury announced it would allocate $20 billion to back a lending facility for the consumer asset-backed securities (ABS) market established by the Federal Reserve (the Fed). The facility, the Term Asset Backed Securities Loan Facility (TALF), is intended to assist the credit markets in accommodating the credit needs of consumers and small businesses by facilitating the issuance of ABS and improving ABS market conditions.

Under the new facility, the Fed will lend up to $200 billion on a non-recourse basis to holders of newly issued AAA-rated ABS for a term of at least one year. The amount lent will be equal to the market value of the ABS less a haircut and will be secured at all times by the ABS. The U.S. Treasury will provide $20 billion in credit protection to the Fed in connection with the facility, using its authorities under the *Emergency Economic Stabilization Act of 2008.* The eligible collateral of the TALF and the transaction structure are as follows:

Eligible Collateral

- Eligible collateral will include U.S. dollar-denominated cash (i.e., not synthetic) ABS that have a long-term credit rating in the highest investment-grade rating category (e.g., AAA) from two or more major nationally recognized statistical rating organizations (NRSROs).
- All or substantially all of the credit exposures underlying the eligible ABS must be newly or recently originated exposures to U.S.-domiciled obligors. The underlying credit exposures of eligible ABS initially must be auto loans, student loans, credit card loans or small business loans guaranteed by the U.S. Small Business Administration (SBA). This may be expanded later to include commercial mortgage-backed securities, non-agency residential mortgage-backed securities or other asset classes.
- Originators of the credit exposures underlying eligible ABS (or, in the case of SBA-guaranteed loans, the ABS sponsor) must have agreed to comply with or already be subject to the executive compensation requirements in section 111(b) of the *Emergency Economic Stabilization Act of 2008.*
- Eligible collateral for a particular borrower must not be backed by loans originated by the borrower or by an affiliate of the borrower.

Transaction Structure

- Credit extensions under the TALF will be in the form of non-recourse loans secured by eligible collateral. Substitution of collateral during the term of the loan will not be allowed. TALF loans will have a one-year term, with interest payable monthly. The term of TALF loans may be lengthened later, if appropriate. TALF loans will not be subject to mark-to-market or re-margining requirements.
- Any remittance of principal or interest on eligible collateral must be used immediately to pay interest due on the TALF loan or to reduce its principal amount.
- Collateral haircuts will be established by the Fed for each class of eligible collateral. Haircuts will be determined based on the price volatility of each class.

Initial market reaction to the TALF program has been mixed. While some are optimistic that it will inject substantial liquidity into the ABS market, many believe some of its restrictions will need to be loosened before that can happen. The one-year loan term and the requirement that the underlying collateral be new or recently originated severely limit the amount of ABS issuance that can be secured by the facility. Furthermore, the program is not able to be utilized by many of the biggest lenders because they can not sell ABS backed by their self-originated receivables, which is most of their production. Additionally, the haircut rate that is used to price the collateral may make it uneconomical if the returns are unattractive.

DBRS recognizes the need for the U.S. Treasury to provide liquidity to financial institutions that provide small business loans and consumer lending such as auto loans, student loans and credit cards and believes that the TALF can jump-start the ABS market if implemented appropriately. As a result, DBRS will continue to participate in industry discussions over the next few months as provisions of the program are finalized and monitor its impact on consumer lending and issuance trends.

For questions or comments, please contact Kathleen Tillwitz at ktillwitz@dbrs.com.