



Five steps to overcome operational challenges when introducing synthetic SRT and CRT strategies for capital efficiency optimization

White Paper

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Introduction

In the ever-evolving landscape of the global banking sector, financial institutions are continuously seeking strategies to optimize capital efficiency while adhering to the complex web of regulatory requirements.

Significant Risk Transfer (SRT) and Capital Relief Trades (CRT) have emerged as pivotal tools within this context, enabling banks to manage regulatory capital more effectively and to foster lending and economic growth.

This thought leadership paper delves into the operational aspects of synthetic SRT and CRT mechanisms, pooling insights from seasoned market players to furnish a comprehensive guide for newcomers on orchestrating these complex financial instruments and processes.

Our objective is to arm bankers and financial organizations with practical knowledge and a strategic blueprint to unlock the myriad benefits of SRT and CRT for capital optimization.

The regulatory landscape

The regulatory framework governing SRT (Significant Risk Transfer) and CRT (Capital Relief Trades) is rooted in the Basel III/IV guidelines, which set forth the capital standards and risk management criteria for banks globally. These instruments are crucial for managing capital ratios effectively while continuing to provide lending services.

For SRT and CRT transactions the following regulation is relevant:

Standardized Transactions and the Basel 3 standard (STC)

The Basel III framework introduces the concept of Securitization of Commercial Risk (STC) standards, which are designed to promote safer and more robust securitization markets. STC criteria focus on

simplicity, transparency, and comparability across securitization products.

The European Simplified Transactions Standards (STS) requirements

Under the regulatory framework, STS securitizations must meet stringent requirements that enhance transparency, standardization, and overall quality of securitization transactions. These include requirements for detailed disclosure on the underlying assets, the structure of the deals, and the parties involved.

Differences between STC and STS

Scope

STC applies broadly to all types of securitization products, while STS is specifically tailored to simpler, more transparent, and standardized products.

Regulatory relief

STS securitizations may qualify for lower capital requirements under certain conditions, unlike STC.

Disclosure requirements

STS requires more detailed and frequent disclosures compared to STC.

SRT and CRT play a critical role within this regulatory context, offering a mechanism for banks to manage their capital ratios more effectively while continuing to provide lending services.

The adoption of securitization simplified with a standardized platform approach

To qualify as STS (Simple, Transparent, and Standardized), securitization transactions must adhere to an extensive set of criteria detailed in Articles 20-22 of the regulatory framework, emphasizing transparency and reporting.

The complexity of these mandates renders manual management unfeasible, spotlighting the necessity for an automated, comprehensive IT solution.

Securitization orchestration platforms revolutionize the securitization operation model, covering the gamut from origination to servicing of asset-backed securities, harnessing cloud technology, AI and automation for a scalable, secure, repeatable and efficient transactional process.

Platform approaches in securitization

Securitization platforms can be broadly categorized into two types: public platforms hosted on cloud services and private platforms deployed in-house, each with distinct advantages:

Public platforms

Hosted on cloud services, offering scalability, enhanced security, and lower upfront costs, accessible from anywhere, ideal for institutions with geographic diversity.

Private platforms

Deployed in-house, providing greater control over security and data management, tailored to the institution's internal processes and compliance needs.

Benefits of securitization operation supported by a platform approach

- Cost and operational efficiencies: leverage know-how and shared resources and competencies
- Scalability and accessibility: repeatable, standardized and proven operational models
- Access to expertise, and support
- Enhanced compliance & risk management
- Continuous updates aligned to regulation updates

Lessons learned from existing deployments

Drawing from a wealth of market experiences, the following section outlines some key lessons learned from banks that have successfully implemented SRT and CRT strategies.

By examining a series of case studies, we identified common challenges faced by these institutions, ranging from

infrastructure setup, data integration as well the selection of assets for transfer to the structuring of transactions in compliance with regulatory standards including reporting.

Through these narratives, we distill a set of best practices for managing the complexities of SRT and CRT transactions, emphasizing the importance of rigorous risk assessment, transparent stakeholder communication, and strategic asset selection.

Infrastructure setup for new clients

In evaluating the deployment environments - on-premise, private cloud, or public cloud - the primary consideration should be the time to market, aligned with the financial institution's overarching cloud strategy.

It is crucial for a platform to be infrastructure-agnostic, enabling seamless operation across diverse environments. Furthermore, the processes for installation and maintenance should be straightforward, minimizing operational complexities.

Leveraging containers and orchestration solutions such as Kubernetes is pivotal in ensuring a low total cost of ownership for these platforms. This approach not only enhances scalability and flexibility but also significantly reduces the burden of ongoing platform management.

While there is a discernible shift towards fully outsourced cloud platforms, financial institutions must navigate the complexities of internal control frameworks. These frameworks, which are primarily concerned with data privacy and adherence to outsourcing regulations, pose a challenge to the wholesale adoption of cloud-based solutions. Despite these obstacles, it is imperative for platforms to be designed with the future in mind, capable of accommodating evolving needs and

operational models to stay ahead in a dynamic financial landscape.

Technical and operational requirements

Technical data integration

Integrating with legacy systems presents a significant challenge for IT and operations teams within financial institutions, often resulting in considerable resource allocation and complexity.

A pivotal strategy to mitigate these challenges involves implementing a versatile ETL (Extract, Transform, Load) layer. This layer facilitates streamlined integration and data manipulation from various sources, including those within legacy systems.

The flexibility of this ETL layer is critical, allowing for configuration-based integration that bypasses the need for extensive custom coding.

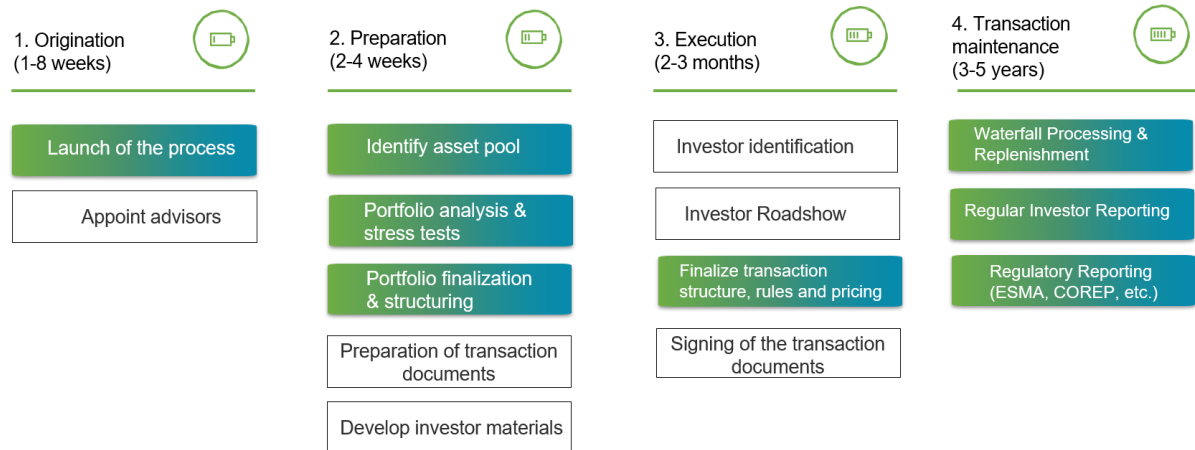
Adopting this configuration-driven approach significantly enhances the system's adaptability to new data sources, while concurrently minimizing the intricacies and expenses tied to data integration efforts.

Such a dynamic and flexible data management framework enables financial institutions to gain a comprehensive and timely perspective of their asset portfolios. This capability is vital for executing informed decisions and advancing strategic objectives efficiently.

Operational setup

The establishment of a robust operational framework is essential for financial institutions, encompassing clear procedures for due diligence, deal structuring, documentation, and the continuous management of SRT/CRT transactions.

This framework should incorporate auditable processes to ensure transparency and accountability, adhering to the "four eyes" principle for enhanced oversight and risk mitigation.



Such a structured approach is crucial for maintaining the integrity and efficiency of transaction management, safeguarding against errors and ensuring compliance with regulatory standards.

Risk assessment framework

Banks engaged in Significant Risk Transfer (SRT) and Capital Relief Trades (CRT) programs encounter substantial hurdles in meeting the Simple, Transparent, and Standardized (STS) criteria. These hurdles include strict adherence to eligibility requirements, robust verification of effective risk transfer, and meticulous management of SRT tests, including documentation of triggers.

A state-of-the-art IT platform stands out as an essential tool in overcoming these challenges. It offers a comprehensive solution for assessing eligibility, documenting risk transfer, and facilitating automated SRT testing. This platform simplifies the compliance and management processes, allowing bankers to ensure that transactions conform to regulatory standards with unparalleled accuracy. The adoption of such technology not only addresses compliance risks but also boosts

operational efficiency and maintains the integrity of SRT and CRT portfolio management. This strategic integration is in perfect harmony with the bank's overarching strategic goals.

Reporting tools

Investing in advanced reporting tools is crucial for efficient and precise regulatory reporting, tailored to the specific needs of financial institutions. These tools should emphasize automation to reduce manual errors and enhance operational efficiency.

These tools should champion automation to diminish manual errors and enhance overall operational efficiency.

Optimal reporting solutions would embody low-code or no-code functionalities, streamlining the reporting process and enabling users to customize and manage reports without extensive technical expertise.

This approach not only simplifies compliance but also empowers institutions



Optimizing capital relief with smart asset selection

In an era of stringent regulatory requirements, financial institutions are increasingly turning to sophisticated asset selection strategies to optimize capital relief. The focus on automation and the integration of advanced IT systems are pivotal in streamlining these processes. Key elements include:

Smart asset selection

Utilizing data analytics to identify assets that provide the most significant capital relief while maintaining compliance with regulatory standards.

Automation

Implementing automated systems to reduce manual intervention, increase accuracy, and speed up processes, thereby enabling more efficient management of asset portfolios.

IT system benefits

Leveraging IT infrastructure to enhance operational efficiency, reduce errors, and facilitate better decision-making through real-time data access and analysis.

Five important steps to achieve a scalable SRT/CRT operation setup

To ensure scalable and efficient operations in SRT and CRT strategies, financial institutions can follow these steps:

Step 1: Robust IT infrastructure

Implement a flexible and scalable IT platform that supports both current needs and future growth.

Step 2: Automation and integration

Use automated systems for asset selection and management to reduce manual workload and increase accuracy.

Step 3: Continuous risk management

Continuously monitor and manage risks associated with SRT/CRT transactions through advanced analytics and reporting tools.

Step 4: Automated regulatory compliance

Stay updated with the latest regulatory changes and ensure all transactions are compliant through automated compliance tools.

Step 5: Training and expert support

Invest in ongoing training for staff and ensure they have access to expert support to manage and optimize SRT/CRT operations effectively.

Conclusion

The transition to the use of a standard platform marks a transformative era in banking securitization strategies.

By embracing platforms and customized support services, banks can achieve unprecedented cost and operational efficiencies, bolster risk management frameworks, and refine their securitization strategies all while significantly reducing the time to launch new transactions.

As the banking landscape evolves, the integration of innovative solutions like securitization platform solutions will be paramount in maintaining a competitive edge and maximizing securitization opportunities, paving the way for a new chapter in capital efficiency optimization.