Securitisation:

A NEW TOOL FOR DESTINATIONS?

Locum Destination Review looks briefly at the use of securitisation in the United States, and wonders whether it might have a bigger role to play in the development of destinations in the UK.

Securitisation is one of those buzz words that is on the tip of everyone's tongue, but which remains a mystery to many. In the United States, it is a garden variety financing tool, used for everything from residential mortgages to New York taxi medallions. Not so yet in the UK, but as the following article by Arvind Bajaj of Morgan Stanley explains, there is good reason for destination owners and managers to be aware of the mechanics and to stay abreast of applications.

So what is a securitisation? Simply described, it is a form of bond financing supported by the cash flow from a single asset or group of assets. It is distinguished from bank borrowing in that is transacted in the public finance markets, and from corporate bond transactions in that the security is provided by the cash flow of the asset(s), not by the underlying creditworthiness of the sponsor.

In comparison to the US, it is safe to say that securitisation in the UK is in its infancy. However, the same could have been said about the US markets only eight to ten years ago. Commercial mortgage-backed securitisations (CMBS), arguably the sector of the market of most relevance to those with property-based assets, grew from $3.6 billion in 1991 to $74 billion in 2001. This is not to say that a similar growth trend in the UK is inevitable, but it does beg the argument.

So why did CMBS take off in the US? As a financing tool, it offered several unique benefits. First, it provided a new way for property owners to access capital at a time when more traditional sources were running scared. Second, it provided bond investors with an investment option characterised by attractive relative yields and diversified risk, the latter by virtue of the rating agencies' stringent diversification requirements. And lastly, the investment banks were quite happy middle-men, participating in underwriting, trading and, where allowed, proprietary investing.

In the following article, Arvind Bajaj provides a primer on UK securitisations and highlights transactions completed for Canary Wharf, Sainsbury's and Punch Taverns, three very different types of destinations. He discusses the mechanics, the rationale and the type of assets and/or business that are candidates for this type of financing.

It is interesting to note the option of securitising businesses in the UK. For a number of years in the US, the rating agencies, as the gatekeepers of securitisations, were quite happy to rate transactions secured by property, but not the businesses that sat atop, at least under the same structures. Those transactions containing KMart properties, for instance, ultimately looked to the creditworthiness (or not, as the case may be) of the corporate parent.

Another interesting market development? The proposed use of securitisation to fuel property development activity, as in the recently announced Canary Wharf transaction, the third in a series. Watch this space ...