Italian CQS securitisation to remain stable as lower risk weights beckon

Lower risk weights for Italian salary and pension-backed loans (CQS loans) will free up lenders' capital, making the product more attractive for financial institutions. But this is unlikely to have a significant impact on overall market volumes or on the number of public CQS securitisations.

The European Parliament approved[1] the reduction in the risk weight for CQS ('cessione del quinto dello stipendio') loans from 75% to 35%, the same level as for residential mortgages. Stronger surveillance by the Bank of Italy and the development of the public CQS ABS market have improved the transparency of this asset class. Even so, CQS loans will not become a widespread direct substitute for consumer loans.

CQS loans can only be extended to employees or to pensioners if borrowers unconditionally authorise their employers or pension providers to make direct payments to lenders by deducting instalments from salaries or pensions. The instalment cannot exceed 20% of the borrower's net salary or pension, and in most cases, the loan is collateralised by accrued severance pay. Additionally, the loans must be insured against death and job-loss events, with direct benefit to the lender[2]. These features help reduce expected losses.

Historical data from originators and from public securitisations indeed show that losses on this asset class are significantly lower than standard consumer finance products. Based on a sample of securitised CQS pools available within the European DataWarehouse repository, the average loss rate is just 0.8%, compared to 4.6% on standard consumer loans and 2.0% on residential mortgages. This is mainly due to the inherent features of CQS loans, which make them safer for lenders.

New rules could release up to EUR 1bn of regulatory capital

The new risk-weights will enter into force in June 2021 and we estimate they could release between EUR 500m and EUR 1bn of banks' regulatory capital, based on the stock of CQS loans as of September 2019 (EUR 19.1bn).

However, in our view, the capital released will not translate into significant growth in the CQS market, with the volume of securitised loans remaining relatively stable in the short term. Around EUR 1.6bn of CQS loans were securitised in 2019, 9.3% lower than the previous year if we exclude the EUR 1.8bn jumbo synthetic securitisation originated by BNL Finance S.p.A.3 (see Figure 3 in the Appendix). Scope does not expect further synthetic securitisations in the future.

Several factors explain why the CQS securitisation market will not develop further in the short term:

1. CQS loans are a niche product, growing at a slower pace than consumer loans.
2. The Bank of Italy has tightened surveillance on financial institutions operating in the CQS market, encouraging higher standards in the underwriting process and requiring more transparency on distribution and brokerage costs.
3. Underwriting and servicing CQS loans requires specific skills compared to standard consumer loans.

[1] Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013.

[2] For more insight on CQS loans refer to Appendix I of Scope's Consumer and Auto ABS Rating Methodology.

[3] For more detail refer to our rating report on Amalia SPV S.r.l.

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Related Research

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CQS loans still a niche product in the consumer finance space

CQS loans struggling to keep pace with consumer loans

The CQS segment represented around 8.8% of newly-originated consumer lending in Italy in 2018 and it has grown at a slower pace than the overall consumer loan market. The volume of CQS loans originated in 2018 grew by 4.6% vs. 2017, but this was lower than the 6.2% increase seen in overall consumer lending.

This divergence sharpened in the first nine months of 2019, with the CQS loans and consumer loans growing, respectively, by 2.6% and 6.3% compared to the same period of 2018.

In terms of product breakdown, 2018 growth in CQS loans came from private employees (+6.8%) and pensioners (+9.8%); the public employee segment fell by 3.0%.

Figure 1: Consumer vs CQS – origination volumes

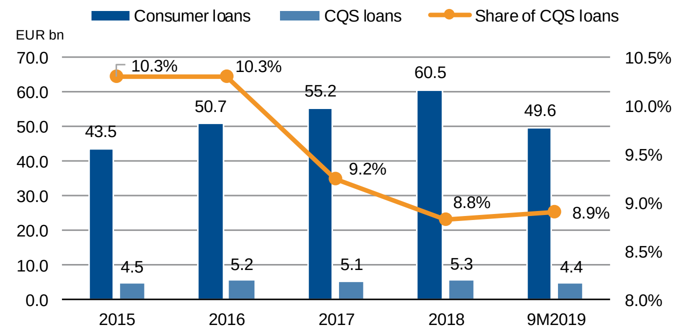
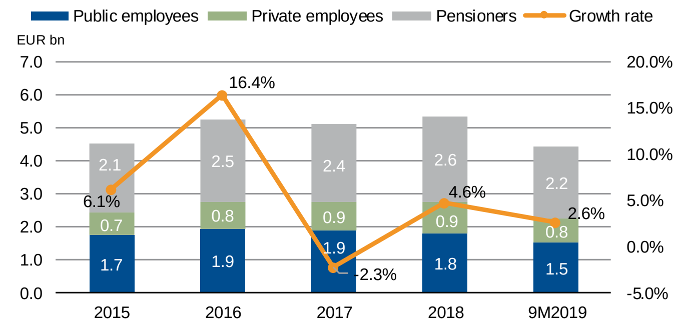


Figure 2: Focus on CQS loans – growth rate evolution



Source: Assofin, Scope

The data suggests that CQS loans are not perceived as a direct substitute for consumer loans. Origination is concentrated mostly within the public segment (i.e. public employees and pensioners representing 83% of total production in 2018), while other economic sectors are not widely covered. Additionally, CQS loans require more guarantees than standard consumer loans, making them less attractive for borrowers (interest rates and other conditions being equal).

Stricter regulatory surveillance aiming to improve lending standards

Stricter Bank of Italy surveillance on CQS lending practices may also have contributed to the slow-down of the market. In 2018, Bank of Italy published its supervisory guidelines[4] to eliminate improper behaviour by operators and increase customer protection.

The guidelines primarily focus on:

i) setting best practices for loan underwriting,

ii) setting higher standards in assessing borrowers' creditworthiness,

iii) improving transparency around distribution and brokerage costs, and

iv) enhancing disclosure requirements.

This has contributed to a slowdown in the origination of new loans, but also to a consolidation of the market, with some operators exiting the segment.

[4] Orientamenti di vigilanza sulla cessione del quinto dello stipendio (March 2018).

I. Appendix. Italian CQS and consumer loans securitisations between 2017 and 2019

Figure 3: Breakdown of securitised pools by originator/sponsor

Principal amount of securitised loans at closing (EUR m)	2017		2018		2019	
Originator/Sponsor	**CQS loans**	**Consumer loans**	**CQS loans**	**Consumer loans**	**CQS loans**	**Consumer loans**
Agos Ducato		2,194.1		2,300.1		2,246.1
BNL / BNL Finance		587.4			1,778.0[5]	
Banca Progetto	110.6					
Banca Sistema	224.5					
BCC Credito Consumo				650.0		
Compass Banca/Futuro		1,500.0	650.0	900.0		900.0
Creditis Servizi Finanziari					172.3	323.4
Dynamica Retail	161.1					
IBL Banca	426.0		1,162.2		1,268.0	
Pitagora	308.1					
Santander Consumer Bank				478.5		595.0
ViViBanca	125.5				204.0	
Total	**1,355.8**	**4,281.5**	**1,812.1**	**4,328.6**	**3,422.3[6]**	**4,064.5**

Source: Scope, European DataWarehouse

[5] Synthetic securitisation transaction.
[6] EUR 1,644.3m excluding synthetic securitisations.

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