

GTR

# Synthetic loans win over investors



**Standard Chartered has closed its first synthetic securitisation of trade finance loans. Known as Sealane, the transaction has proved resilient despite turbulence in the Asian structured trade finance market. Rebecca Spong examines the deal.**

Facing a rocky market for structured finance deals in Asia, Standard Chartered Bank (SCB) has managed to complete its first synthetic securitisation of trade finance loans, and upsized the transaction from US\$2.5bn to US\$3bn. Lehman Brothers also arranged and distributed the transaction. Paul Hare, managing director, portfolio management, at SCB remarks: "It is the first time this type of trade finance lending product has been made available to this investor base in this form in meaningful size." Tan Kah Chye, global head of trade finance at SCB, adds: "StanChart's credit expertise helped make this deal such a success. We understand our customer base and we understand our core markets."

## From the Start

The deal structure draws much from SCB's already established collateralised loan obligation (CLO) programme known as Start CLO.

Previous transactions completed under this programme involve securitisations

of unsecured debt obligation portfolios, and the first deal was closed at US\$2bn in November 2005. This was followed by the US\$1.6bn Start II CLO closed in June 2006, a US\$1.5bn Start III CLO closed in December 2006, and a US\$1.5bn Start IV CLO in June 2007. Commenting in a statement, Matthew Geason, group head of portfolio management, observes: "Sealane represents an evolutionary step in Standard Chartered's balance sheet securitisation programme. Our award-winning Start CLO transactions have earned us an enviable track-record for high quality balance sheet issuance. "Bringing a new product to market – on

schedule and upsized – in the current environment represents a considerable achievement and perfectly observes the power of Standard Chartered's franchise."

## Effective portfolio managing

The evolution of the Start CLO programme towards trade finance loan securitisation is seen as a natural development in terms of the bank looking for new ways to better manage its portfolio.

Hare says: "After the bank's loan portfolio, the next biggest user of wholesale bank balance sheet is short-term trade finance. So trade was the next logical target after our successful Start CLO programme. We began discussions about a possible trade finance securitisation over a year ago."

The key difference with using trade finance loans as the underlying collateral of the deal is short tenors involved, as the loans are linked to actual trade flows of goods. The short-term tenors improve the underlying quality of the risk.

"Standard Chartered finances huge volumes of trade flows, but the majority of these financings have short-term tenors of just 60 to 90 days," explains Tan.

Having it all on balance sheet is a cost to me. The securitisation programme is a way of creating further capacity for increased trade finance business

Hare adds: "The structure is very innovative. It is a hybrid CLO-ABS structure. We wanted to give investors the full benefit of the short-term nature of this asset class – but as a three-and-a-half-year investment. In effect, the investor is taking a rolling 90-day view on these markets. This proved very popular."

Through the transaction, Standard Chartered has sold

the credit risk of a diversified pool of 13,000 trade finance loans extended to over 1,500 borrowers across 23 countries. The pool

of obligors features almost 80% Asian exposure, of which over 50% were from high growth local corporate sector.

### Creating trade finance capacity

Looking at the deal from a trade finance perspective, Tan views this synthetic securitisation as a great opportunity to free up some capacity to further boost SCB's trade finance business.

The bank has already seen huge amounts of trade finance business going through its books, with its level of business reflecting global and Asian market trends.

Merchandise trade for 2006 grew by 8%, according to World Trade Organisation

### Structuring the deal

The issuer of the transaction is an SPV known as Sealane (Trade Finance), incorporated in the Cayman Islands. Various credit notes are issued to investors through this entity.

In total there are five different tranches available to investors. There is a US\$60mn Class A tranche, rated AAA and paying 90 basis points. The Class B tranche is also US\$60mn, rated AA and pays 160bp, while Class C tranche is for US\$60mn is rated BBB and pays 230bp.

A US\$30mn Class D tranche has also been issued, rated BBB and pays 400bp. The US\$120mn E tranche or sub-notes are unrated.

Although the total transaction amounts to US\$3bn, only US\$330mn-worth of credit notes were issued into the market. SCB kept a US\$30mn tranche on its books as a first loss. The remaining balance of US\$2,640mn was kept on the bank's books in the form of a credit default swap (CDS), with the bank as a protection buyer paying a fee to a protection seller to protect its outstanding balance in case of default.

### Pricing decline

Despite the popularity of the deal, the spreads being paid have widened since the last Start CLO transaction completed by SCB. Yet, this is being taken not as a reflection of the product, but rather a reflection of market trends. The lower pricing has also not put off the bank from arranging this transaction or potentially similar deals in the future.

Geason explains in a statement: "Although spreads have widened considerably since our last Start transaction in June, we believe that suspending distribution activities simply because markets have moved is counter-intuitive."

Hare says to GTR: "One of the key challenges we faced was educating investors on the underlying trade finance assets. It was a new product for most of them, but once they got to grips with it, they loved the story."

The transaction could well be used as a template for other banks in Asia looking at methods to better and more efficiently manage their balance sheets.

Tan concludes: "From our perspective, this is not a one-off transaction. Sealane will become a programme, like Start. We will also look at other innovations. It may not be simple repeat issuance."



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Tan Kah Chye  
Standard Chartered

(WTO) statistics, and this development is mainly being driven by economic growth in Asia, led by China and India.

Given the robust strength of world trade and SCB's position in the Asian market, inevitably the bank is keen to further expand its trade finance capabilities. Expanding its trade finance business is also a strategic move, as securing the trade business of a client can often be the first step in securing the client into other financing programmes offered by the bank.

However, despite the expanding pool of trade business, SCB is reluctant to leave itself too overexposed by taking on too much risk.

"We needed to more efficiently distribute the risk of the trade finance portfolio. Having it all on balance sheet is a cost to me. The securitisation programme is a way of creating further capacity for increased trade finance business," states Tan.

The various tranches were rated by both Moody's and Standard and Poor's. SCB is retaining a US\$30mn tranche as a first loss. It will absorb the first 1% and under of potential losses, and by doing so aims to improve investor confidence in the strength and quality of the transaction.

By acting as a form of 'buffer' to take on any initial losses, the bank is encouraged to ensure the bundle of loan obligations is made up entirely of good quality risks. Using this form of structure will mean that SCB itself, rather than the investors, will take the first hit in the event of potential defaults. Any subsequent losses will be absorbed by the unrated sub-notes, taking any losses 4% or under.

The D Class notes will absorb the next 1% of losses, and the C Class notes take the next 2%. The B Class notes will then take the subsequent 2% of losses, and investors in the AAA rated notes will not be affected by any losses until the first 10% of losses have been absorbed by the lower-rated tranches.

### Deal information

**Deal name:** Sealane

**Issuer:** Sealane (Trade Finance): incorporated in Cayman Islands

**Lead arrangers:** Standard Chartered and Lehman Brothers

**Amount:** US\$3bn

**Replenishment period:** 3 years

**Scheduled maturity:** 3.5 years

**Pricing:**

Class A (rated AAA) – 90bp

Class B (rated AA) – 160bp

Class C (rated A) – 230bp

Class D (rated BBB) – 400bp

Class E/sub-notes – not rated