

vdp Transparency Initiative

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Due to its simple design, Pfandbrief is one of the most transparent capital market products. In contrast to different tranches of a securitization transaction one may look through the Pfandbrief structure at the underlying cover assets. Pfandbrief issuers want to expand and carry further their market's transparency with their voluntary initiative that goes beyond legal demands stipulated in the Pfandbrief Act. Providing individual and aggregated data disclosed on the grounds of Art. 28 Pfandbrief Act vdp member banks and their association contribute to this goal.

BODO WINKLER | Association of German Pfandbrief Banks

1 Background

In spring 2007 the US subprime crisis erupted in the capital markets. The US was the first to be hit but as the turmoil spread the European securitisation markets were also affected. Three years later there is still hardly any market for structured products on either side of the Atlantic. Investor distrust is obviously extremely deep-seated. A frequently cited reason for this is the overly positive ratings that securitisation issues received from the rating agencies. Given the extremely complex structures of some of these instruments, many investors relied solely on these ratings when making their investment decisions – telling proof of how lack of transparency can foster distrust.

The Pfandbrief has a much simpler structure than financial instruments such as MBSs or CDOs. In addition the uniform legal framework ensures that the same quality standards apply to all Pfandbrief and that the investor is protected by a tight-meshed safety net. The simplicity and transparency of the Pfandbrief represent significant advantages and not only compared with the structured instruments mentioned above. Against this backdrop, investors have increasingly expressed their concern to the vdp that they should be provided with still better resources to analyse Pfandbrief cover pools extensively themselves, thus reducing the dependence on rating agencies in this segment. Art. 28 of the Pfandbrief Act (PfandBG) provides the legal basis that defines which information issuers are required to publish regularly on the cover pools and the volume of Pfandbrief outstanding. These include

- The total volume of Pfandbrief outstanding as well as the related cover pools in terms of nominal, net present value and stressed net present value;
- The share of derivative financial instruments in the cover assets;
- The share of further cover assets;
- The maturity structure of the Pfandbrief and cover assets;
- Information on the granularity of the cover assets;
- Information on the mortgages by
 - type of usage of the financed property
 - region/state;
- Information on the claims against of the public sector by
 - state
 - type of issuer
- Information on the ship mortgages /aircraft registered liens by register country;
- Information on non-performing cover assets.

Investors appreciate these so-called transparency requirements since it gives them security in terms of the frequency and scope of the reports. Of all covered bond legislations, only the German Pfandbrief Act and Greek Covered Bond law grant investors an enforceable right to receive clearly defined data relating to the cover assets. In the opinion of the majority of investors the information pursuant to Art. 28 PfandBG is sufficient to enable appropriate analysis of the structure of a cover pool and to assess the risks associated with an investment adequately.

However, investors found that the presentation of the reports of individual issuers were as different from each other in some cases as their design and positioning on the websites of the issuers. In addition, the reports were usually available in PDF format only so that there was no possibility for investors to process them electronically for their own further analysis in any standard way.

The information provision to investors is of great importance for the member banks of the vdp. The vdp Committee for Pfandbrief and Capital Market Issues therefore decided in June 2009 that Art. 28 reports of the vdp member institutes should in future be published on the vdp website in a uniform format that could subsequently be electronically processed in addition to their presentation on the websites of the institutes. This was the starting shot for the vdp Transparency Initiative.

Since then the working group Art. 28 PfandBG has set about defining the initiative in concrete terms. Three key issues were identified:

1. Development of a uniform understanding of the requirements of Art. 28 PfandBG;
2. Design/layout of the reports and the time frame for their submission;
3. Transfer of member banks' data to the vdp.

The transfer of member banks' data to the vdp is a purely technical issue and as such it suffices to say here that the existing vdp statistics system will be used for this. The association already uses this system to generate its real estate statistics and the aggregated statistics relating to Art. 28 PfandBG.

The items "uniform understanding" and "layout", however, are likely to be of particular interest for all those at whom the transparency initiative is directed.

2 Uniform understanding of the requirements of Art. 28 PfandBG

Some requirements of Art. 28 PfandBG were interpreted differently by some issuers in the past. In order to facilitate a better comparison of the reports for investors, it is therefore important to identify such requirements. Following that, a binding recommendation needs to be drawn up in each case as to how vdp members should deal with the respective requirement in future. The following describes the most important of these in brief.

Art. 28 para. 1 no. 1

Report of the stressed net present value of Pfandbrief outstanding and/or the respective cover pools

Only one stressed net present value each for assets and liabilities is to be reported. This should be the one stressed net present value which produces the lowest over-collateralisation amount. Every issuer should disclose whether they use the dynamic or static approach and/or an internal model to calculate the stressed net present value.

Art. 28 para. 1 no. 2

How to deal with floating-rate loans

Floating-rate mortgage loans should be allocated to the maturity bands based on the date of the next margin adjustment, while the adjustment date of the underlying reference interest rate should not be used as a basis.

How to deal with redemptions of cover assets

Allocation to maturity bands should be based on the scheduled redemption tranches, applying a cash flow approach.

Maturity structure of Pfandbriefe outstanding: Pfandbriefe where the bank has a call option

It is not necessary to take a call option into consideration since it is the Pfandbrief bank and/or the cover pool administrator, who decides whether to exercise them.

Fixed interest rate terms for cover pools: Cover assets where the bank has a call option

Allowance for call a option of the bank can be made on the asset side.

Art. 28 para. 1 no. 3

Reporting on derivatives

Interest rate derivatives are stated at their net present value netted over all master agreements. This means that only one net present value is stated, either as a liability or an asset, per type of Pfandbrief.

Art. 28 para. 2 no. 1 a

Reporting on the cover assets of Mortgage Pfandbrief by lending volume

Only regular cover assets should be reported.

Art. 28 para. 2 no. 1c

Segregation of residential and commercial real estate

The assets must be segregated solely according to their usage. It is insignificant on the other hand whether the borrower is a natural or legal person. This form of segregation is dealt with identically throughout the official statistics and reflects the different markets on which properties are bought and sold.

Para. 3 no. 1

Treatment of bank securities that do not constitute further cover assets pursuant to Art. 20 para. 2 PfandBG

Claims against agencies and/or Landesbanks (grandfathering) must be assigned to the category “other public-sector borrowers”. It is planned that they will be reported in an “of which” position.

As far as content is concerned, the transparency initiative meets all the requirements of Art. 28 PfandBG. There are no current plans to publish uniform key figures on cover pool assets that go beyond the provisions of the law.

3 Design/layout of the reports and time frames

Publication according to section 28 para. 1 nos. 1 and 3 Pfandbrief Act
Pfandbriefe outstanding and their cover | Q4 2009

Outstanding total		nominal value		net present value		risk-ad
		Q4 2009	Q4 2008	Q4 2009	Q4 2008	Q4 2009
Mortgage Pfandbriefe	(€ mml.)	215.142,0	204.238,2	227.233,1	214.289,8	230.380,7
of which derivat	(€ mml.)	-	-	78,9	16,3	2,4
Cover Pool	(€ mml.)	266.274,2	245.127,4	284.071,6	266.749,8	282.490,7
of which derivat	(€ mml.)	2,0	1,1	639,2	933,6	48,1
Over-Collateralised	(€ mml.)	51.132,2	40.889,2	56.838,5	46.507,8	52.110,0
OC in % of Pfandbriefe outstanding		23,8	20,0	25,0	21,7	22,6

Outstanding total		nominal value		net present value		risk-ad
		Q4 2009	Q4 2008	Q4 2009	Q4 2008	Q4 2009
Public Pfandbriefe	(€ mml.)	470.409,4	557.087,4	497.853,8	549.779,3	479.896,6
of which derivat	(€ mml.)	-	11,0	180,7	887,8	85,9
Cover Pool	(€ mml.)	539.389,9	616.611,1	572.979,0	654.859,3	548.803,1
of which derivat	(€ mml.)	5,2	6,8	724,5	509,5	84,7
Over-Collateralised	(€ mml.)	68.980,5	59.523,7	75.125,2	76.788,8	68.906,5
OC in % of Pfandbriefe outstanding		14,7	10,7	15,1	12,1	14,4

Example: aggregated data pursuant to Art. 28 para. 1 nos. 1 and 3 PfandBG in the new layout

The reports will be published on the vdp website (www.pfandbrief.de) under “Statistics”. Publication starts with the figures for the 2nd quarter of 2010. At the end of every quarter the Pfandbrief banks have two months in which to transfer the data for the quarter just ended to the association. For the last quarter of the year the period allowed is 3 months due to the preparation of the annual account closing which also contains the Art. 28 numbers. Since the current draft of the PfandBG revision specifies a legal deadline of one month for the quarters I–III and two months for quarter IV, it is possible that the deadline for transfer to the vdp will also be similarly reduced. In either case, the first publication is planned for mid-September of this year. So that a data history is available for every institute right from the start, not only the reports for the second quarter 2010 will be published, but also those for the periods ending December 31, 2009 and March 31, 2010. Since every report always contains the respective prior-year figures for comparison purposes, the vdp website will thus have data available that goes back to December 31, 2008.

The reports of the banks will be structured identically in each case and will have a uniform layout. They will be offered in three formats: PDF, xls and csv. The PDF variant is considered a reading version. The two other formats are suitable for further direct processing. To enhance usability for as many investors and other interested persons as possible, two different options

will be offered. Ahead of the first publication of the transparency data, a dummy version of the csv file has been available on the vdp website since July that enables interested parties to create the necessary links to their own databases.

The website will offer sorting possibilities for the reports both by reporting date and bank name. The xls and PDF versions contain the respective provisions of Art. 28 PfandBG that underlie the data. The reports will be available in both English and German. At the request of vdp member banks the reports of the individual institutes will not contain any graphs. The aggregated reports of the association will, however, incorporate graphs.

The Pfandbrief banks that form the membership of the vdp are convinced that the transparency initiative will make a further contribution to improving the information provided to investors on their issues. They are also aware that the demand for information is likely to increase. They will therefore not cease in their efforts to further improve transparency. By making available an extensive range of transparencies data in uniform formats, in a central repository and based on a uniform understanding of the content, the vdp banks are once again setting a benchmark in the European covered bond market. It would be indeed desirable if this transparency level were to set a precedent for other covered bond jurisdictions. The Pfandbrief issuers also remain committed in future to their aim of being standard-setters for transparency within the covered bond universe.