

*A presentation to:*

**TEXPERS**

**August 24, 2009**



*For Use Only at the TEXPERS Summer Forum. Not for Further Distribution.*

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### POTENTIAL BENEFITS OF SECURITIZATION

#### Key Features of Securitization

- Segregate pool of assets in bankruptcy remote special purpose vehicle
- Create bonds from the assets' cash flows: reallocate credit risk/cash flow timing

#### Benefits to ISSUERS:

- Create bonds with ratings higher than corporate debt
- Capital relief (off-balance sheet accounting)
- Gain-on-sale accounting (not always)

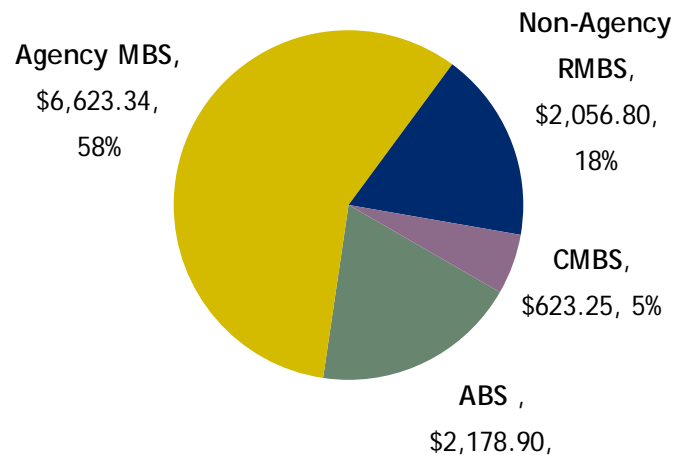
#### Benefits to INVESTORS:

- Bonds that meet preferred habitat: risk profile (primarily AAA) and timing
- Corporate risk vs. secured claims to real assets
- Diversified pool to help reduce idiosyncratic defaults

## Securitized Assets: Past, Present, and Future

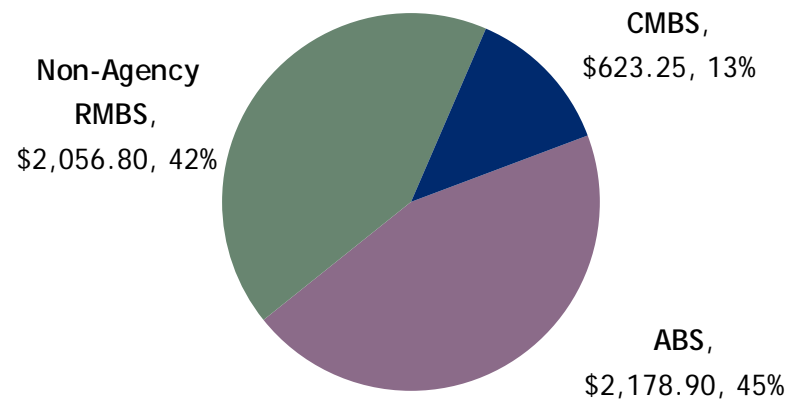
### A MAJOR ASSET CLASS IN THE US BOND MARKET (Par Outstanding)

Securitized Universe - \$11T



33% of Bond Universe

Non-Agency Securitized Universe - \$4.8T

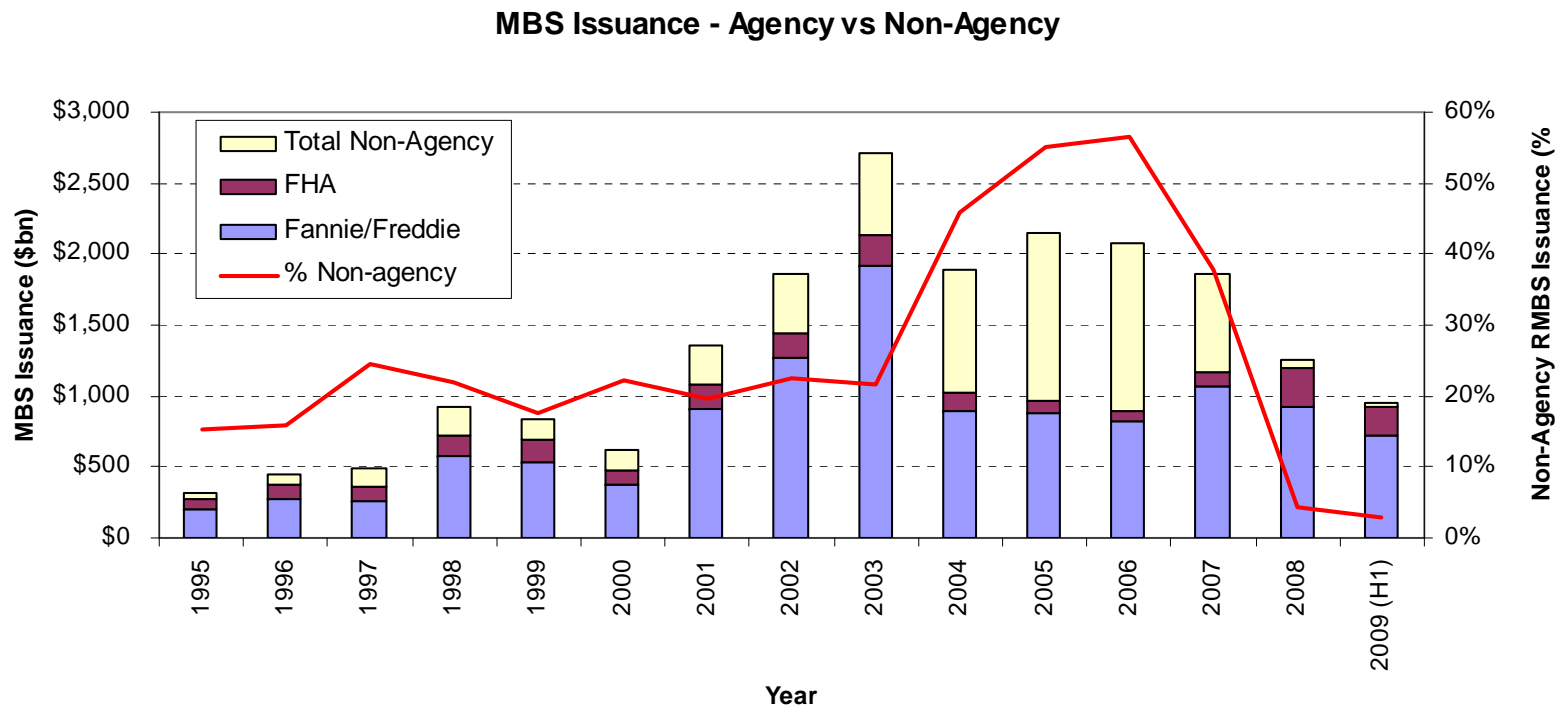


40% of Credit Sensitive Bonds

Source: SIFMA, Federal Reserve Flow of Funds, Standard & Poor's. Bonds par outstanding as of Q2:2009. ABS includes CDOs. Figures shown in billions

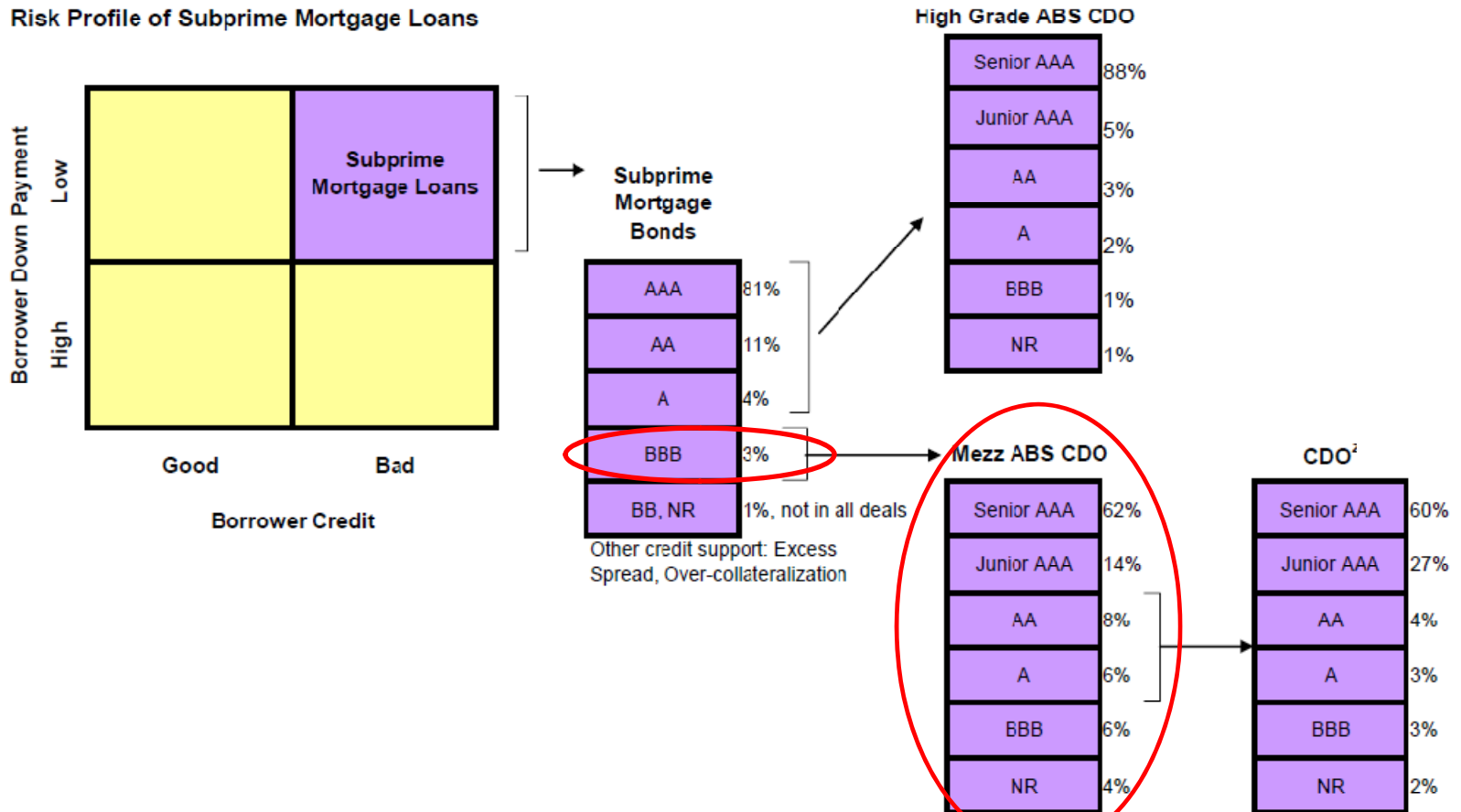
## EXPLOSIVE ISSUANCE OF NON-AGENCY RMBS

Non-Agency MBS Issuance: from \$203B in 1998 to \$1,170B in 2006



Source : Inside MBS & ABS, Loan Performance, Amherst Securities

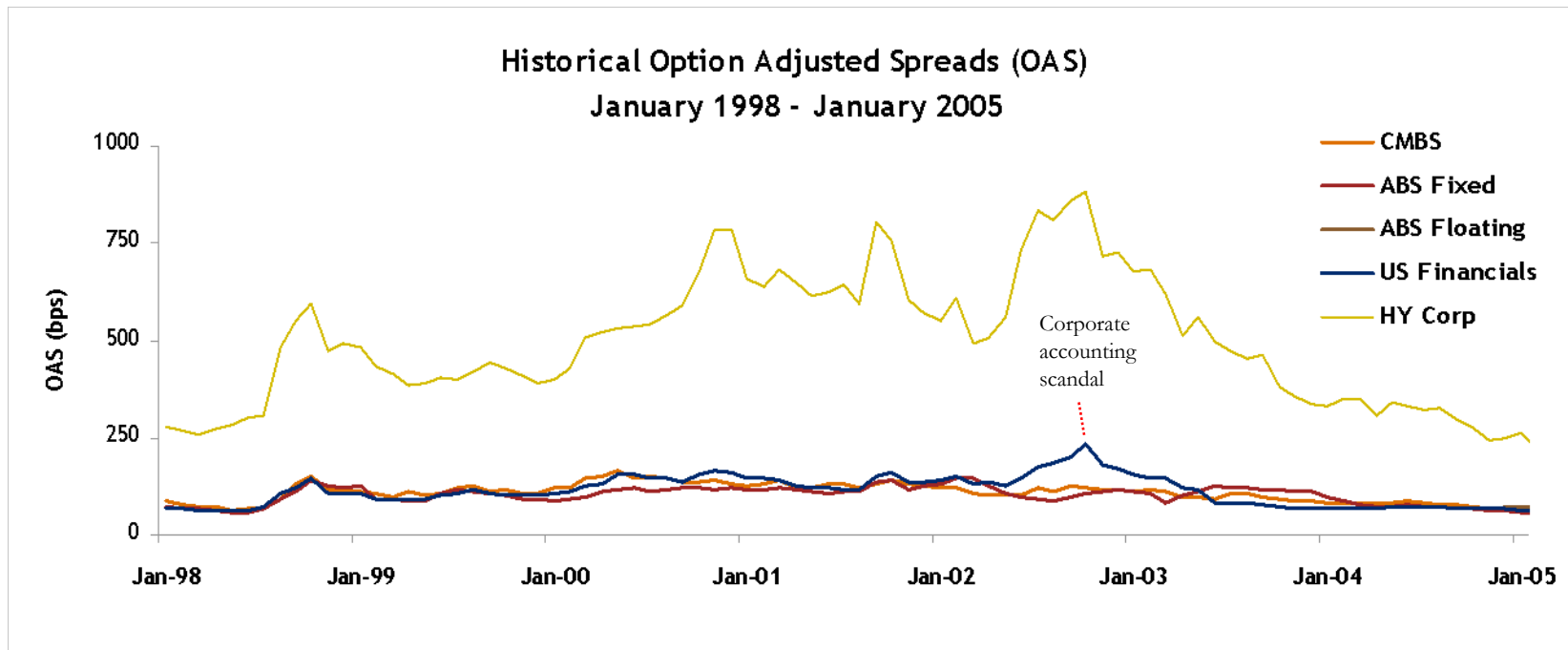
CDOs: TURNING SUBPRIME LOANS INTO AAA-RATED BONDS



Source: UBS Chart highlights transformation of BBB-rated bonds into AAA-rated CDOs

## Securitized Assets: Past, Present, and Future

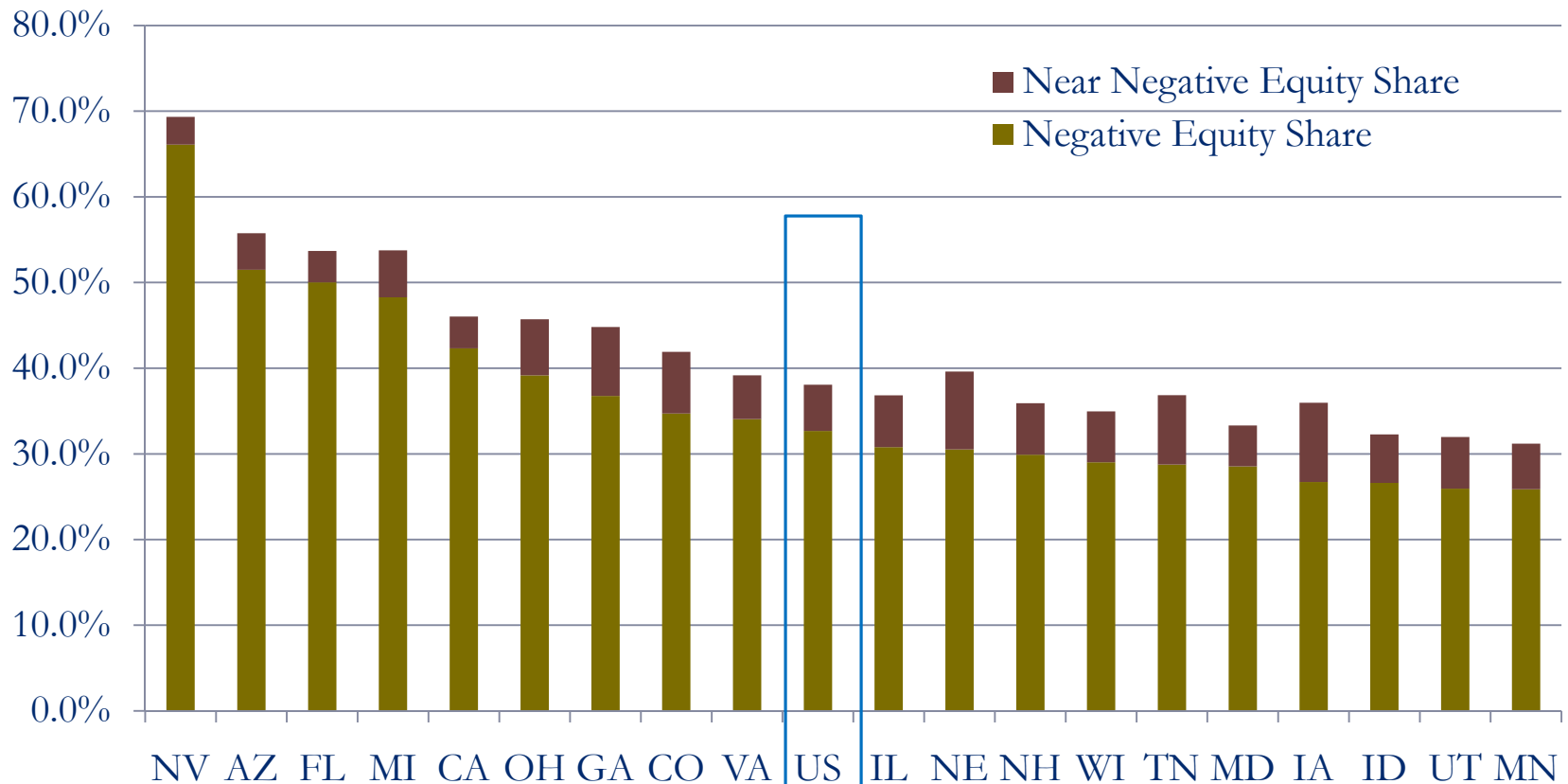
### SECURITIZED CREDIT SPREADS PROVIDED RELATIVE SAFE HAVEN IN PRIOR RECESSION



Data Source: Merrill Lynch Indices, monthly data. See slide 9 for data through 7/31/2009.

## Securitized Assets: Past, Present, and Future

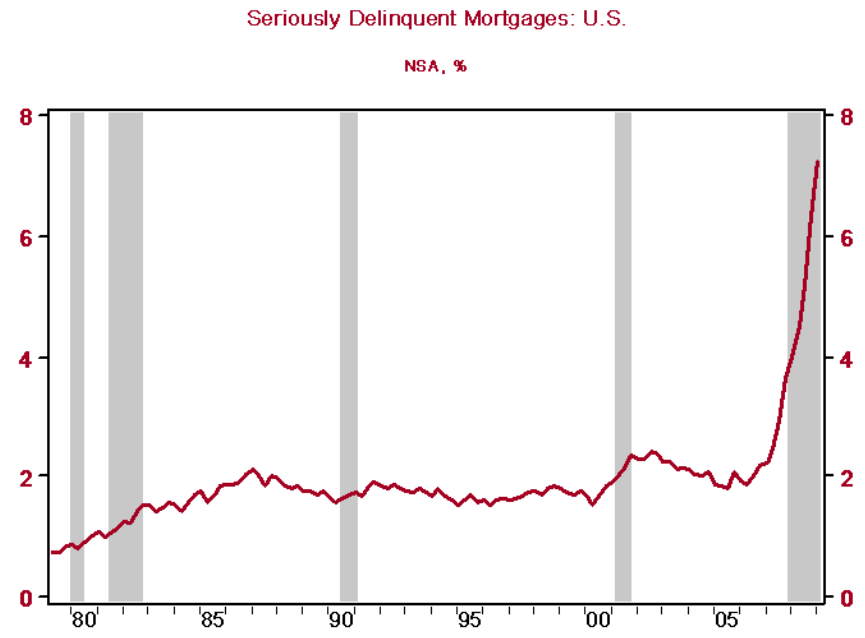
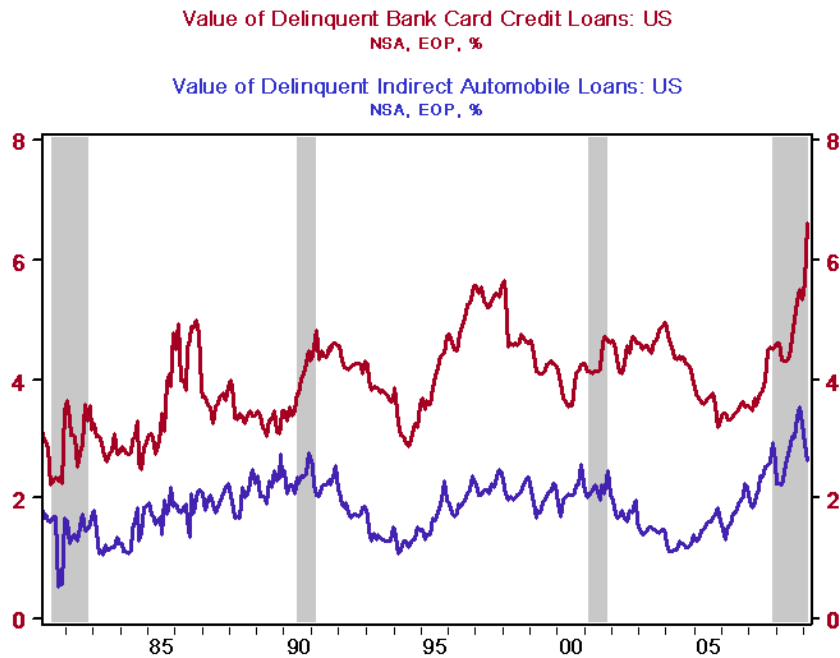
### THE PROBLEM OF NEGATIVE EQUITY ONE THIRD OF US MORTGAGE BORROWERS ARE "UNDERWATER"



Source: First American CoreLogic, data as of 2Q09

# Securitized Assets: Past, Present, and Future

## CONSUMER CREDIT PERFORMANCE: A LONG TERM PERSPECTIVE

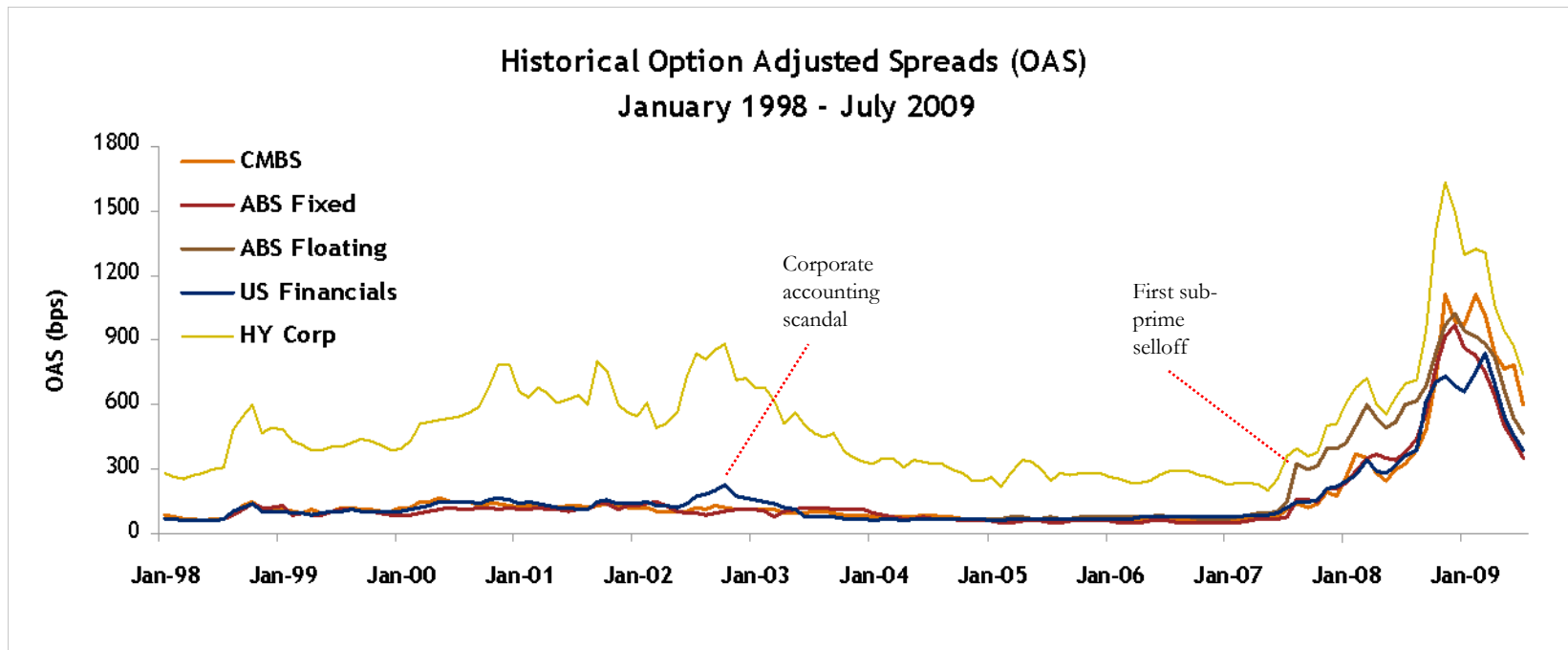


- Debt burden is 0.2-0.3x income
- **Primary driver: employment**, tested in several previous recessions
- Average life: 1-4 years, 6 years legal max

- Debt burden is 3-6x income
- **Primary driver: house prices**, never tested in nominal house price decline environment
- Average life: 3-12 years, 30 years legal max

## Securitized Assets: Past, Present, and Future

### SECURITIZED CREDIT SPREADS BEHAVED LIKE HIGH YIELD DEBT IN CURRENT RECESSION



	US				
	CMBS	ABS Fixed	ABS Floating	Financials	HY Corp
<b>1998-2007 Avg</b>	101.80	94.96	117.08	108.11	440.14
<b>1998-2007 Std Dev</b>	101.34	113.10	327.71	137.05	598.48
<b>7/31/2009</b>	604.00	355.00	464.00	390.00	743.00
<b>Std Dev above Normal Avg</b>	4.96	2.30	1.06	2.06	0.51

Data Source: Merrill Lynch Indices. Monthly data as of 7/30/2009. ABS Floating OAS data only available from 12/04.

### GOVERNMENT PROGRAMS TARGET THE SECURITIZED SECTOR

#### Term Asset-Backed Securities Loan Facility (TALF)

- Non-recourse, non-mark-to-market leverage to buyers of Eligible New Issue AAA ABS
- Expanded to Legacy and New Issue AAA CMBS
- Non-Agency RMBS is NOT included in TALF

#### Agency (GSEs)-related programs

- Facilitate refinancing of Agency MBS to higher loan-to-value borrower (80-125% LTV)
- Government purchase of agencies debentures and MBS

#### Home Affordable Modification Program (HAMP)

- Standardized modification approach to be followed by most servicers
- Servicers are paid an incentive fee

#### Public-Private Investment Partnership (PPIP)

- Leverage and matched-equity to purchase broad range of Legacy Assets (not limited to AAA securities)

## THE FUTURE OF SECURITIZATION

### Traditional Benefits of Securitization

- Create bonds with ratings higher than corporate debt
- Capital relief (off-balance sheet)
- Gain-on-sale accounting (not always)

### Estimating The Future

- This key benefit should be preserved for the originate-to-retain model
- Most deals will be on-balance sheet
- Gain-on-sale greatly diminished
- The future of GSEs needs to be clarified

**Government Intervention and Regulation  
Will Largely Shape the Future of the Industry**

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### BIOGRAPHY

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Alessandro Pagani is vice president of Loomis, Sayles & Company and senior securitized asset strategist for the Loomis Sayles fixed income group. Alessandro leads his team in developing investment strategies for all mortgage pass-through, asset-backed, and commercial mortgage securities as well as other related structured fixed income investments. With 11 years of investment management experience, Alessandro joined Loomis Sayles in 2008 from Cambridge Place Investment Management where he worked as co-head of global research and credit. Alessandro also worked as director of asset-backed securities research at Banc One Capital Markets. He earned a doctoral degree in economics and commerce from the University of Brescia in Italy.