11th November, 2013

To
Division of Foreign Institutional Investors and Custodians
Investment Management Department,
Securities and Exchange Board of India,
Plot No. C4-A, "G" Block,
Bandra Kurla Complex,
Bandra (East) Mumbai - 400 051
India

Sub: Representation for permitting Foreign Institutional Investors to invest in asset backed securities

Respected Sir,

About the Indian Securitisation Foundation (ISF)

ISF is a not-for-profit entity representing the securitisation industry in India. The membership of the Foundation includes banks, NBFCs, microfinance institutions, other issuers and investors and securitisation professionals for promoting interest of securitisation and fixed income securities in India.

Typical investors in securitisation include public sector banks, private sector banks, mutual funds, insurance companies and others. Currently Foreign Institutional Investors (FIIs) have not been permitted to make investments in asset backed securities in India under the extant SEBI (Foreign Institutional Investors), Regulations, 1995. However, FIIs can invest in security receipts issued by asset reconstruction companies. While, it may not be incorrect to say what ABS is to securitisation of standard assets, security receipts (SRs) are to non-performing assets, the rationale for not permitting FIIs to invest in ABS yet permit them to invest in SRs in not known.

Similarly under the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000 investment in SRs issued by asset reconstruction companies is permitted but ABS is not permitted.

As ISF is dedicated to the cause of promoting securitisation in India, we humbly submit our representation herein below on permitting FIIs to invest in securitised instruments.

Our representation

Based on our understanding of the extant SEBI and RBI regulations[1] with regard to investments by FIIs in equity and debt securities, we humbly submit that currently investment

[1] Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000

in ABS has not been permitted to FIIs. However, investment in SRs issued by asset reconstruction companies is permitted under the RBI regulations.

While the intent of the lawmakers is well placed to allow FIIs to invest in SRs and other securities, however the intent could not have been to keep away FIIs from investment in securitised paper.

Recently, SEBI has expressed intent to amend the extant regulations to usher the FPI regime and SEBI in its board meeting held on 5th October, 2013 has approved the draft SEBI (Foreign Portfolio Investors) Regulations, 2013 ("**FPI Regulations**"). Incidentally in these regulations as well, ABS has been given a miss from permitted investments' list.

Investment in ABS will not only provide broad basing of investors in the securitisation market but will also promote issuance of papers ranging from medium term to a long term based on the underlying assets cashflows and more and more of asset classes can be securitised and will result in widening participation in the market. As a fixed income security, which is typically AAA rated and offering good returns, we would request you to permit FIIs to invest in ABS as well. Further, keeping in line with the government's efforts to promote bond market in India, healthy market for fixed income securities has securitised debt instruments as an important component.

We request that the amendment be effectuated by:

a. An amendment to the extant SEBI regulations including ABS as an permissible investment; OR

b. Where the FPI Regulations are to come into effect, include ABS as permissible investment in the FPI Regulations.

Below we list down few of the reasons incentivising FIIs to invest in ABS:

a. FIIs investment in India, specifically to in debt securities has seen a sharp decline due to macro-economic factors, regulatory uncertainty, socio-political factors etc. ABS is a well understood and acceptable asset class internationally. Permitting investment in Indian ABS would attract FIIs investment into India as it will be a familiar ground for them.
b. FIIs are looking for suitable investments in fixed income securities. Asset backed securities are fixed income securities, and provide an effective alternative to traditional corporate bonds.
c. Asset backed securities have more diversification underlying the instrument than corporate bonds. Hence, investments in asset backed securities may be considered safer as compared to corporate bonds, which is an exposure in a particular corporate.
d. Asset backed securities typically are rated, and ratings are quite often independent of the rating of the issuer. Many asset backed securities have attained AAA ratings which have withstood the test of time.
e. Asset backed securities represent portfolios of loans which in turn go for several productive investments such as infrastructure, SME lending, equipment finance, etc. Each of these sectors have multiplier impact for the country.

Based on the above rationale, we humbly submit that FIIs be allowed to make investment in ABS.

Also with this representation, find enclosed **Annexure I** detailing the current state of the securitisation market, extant regulations applicable to securitisation transactions in India and the investment regulations applicable to FIIs.

Should you need any further clarification, we would be glad to provide the same.

Thanking you,
Yours truly,
For ***Indian Securitisation Foundation***

Cc to:
The Chief General Manager
Reserve Bank of India
Central Office
Mumbai -- 400001

Nidhi Bothra

Annexure I

Securitisation market in India

Securitisation as a financial instrument has been prevalent in India since 1990s. The securitisation market started with innovative structures and was largely dominated by PTCs scaling new peaks in terms of volumes of issuances every year. Thereafter the Securitisation Guidelines issued in 2006 (2006 Guidelines[2]) was heavy on regulating the PTCs and the entire market shifted to bilateral assignments as the 2006 Guidelines were not applicable to bilateral assignments.

Securitisation market in India was never strong and has been affected more by internal issues than by external shocks. In the wake of the sub-prime crisis, the RBI took cues from the global regulators and felt the need for an overhaul of the securitisation regulations in India. A revised draft of the guidelines was placed on the website of the RBI in September 2011. Thereafter on 7th May, 2012, RBI issued the Revised Guidelines on Securitisation Transactions[3] (2012 Guidelines). The 2012 Guidelines lay down separate guidelines for Securitisation and Direct Assignments unlike international regulations that lay down single criteria for transfer of assets whether to SPV or any other real life entity. Post the 2012 Guidelines the market seemed to have shifted back to the PTCs route.

The recent most regulatory development has been the Finance Act, 2013 providing relief to certain class of investors in securitisation by introducing Chapter XII-EA in the Income Tax Act, 1961 with regard to special provisions relating to tax on income distributed by securitisation trusts.

In terms of volumes, the market composition of the structured finance products has been such that ABS has been dominating the market over years. The tabular presentation on the volumes of securitization in India is as below:

	FY 2008		**FY 2009**		**FY 2010**		**FY 2011**		**FY 2012**	
	Amount	Share	Amount	Share	Amount	Share	Amount	Share	Amount	Share
ABS	31,323	49%	13,581	25%	21,497	50%	20,920	68%	26,071	71%
RMBS	588	1%	3,291	6%	6,254	14%	5,029	16%	7,680	21%
Total Retail Securitisation	31,911	50%	16,872	31%	27,751	64%	25,948	84%	33,751	92%
LSO	31,819	50%	35,608	66%	14,581	34% %	4,341	14%	2,217	6%
Others	--	--	1,160	2%	787	2%	536	2%	635	2%
Overall total	36,730	100%	53,640	100%	43,118	100%	30,825	100%	36,603	100%
Growth	73%		(16%)		(20%)		(29%)		15%	

Source: Data collated from ICRA's estimates

In terms of volumes the market has securitised loans worth Rs. 36,603 crores in the financial year 2012-13. In the year 2012 securitisation volumes have grown 15% from the last fiscal

[2] http://rbi.org.in/scripts/NotificationUser.aspx?Id=2723&Mode=0

[3] Revisions to the Guidelines on Securitisation Transactions, May 7, 2012, http://rbi.org.in/scripts/NotificationUser.aspx?Id=7184&Mode=0

and after a continuous decline in volumes for the last three years. The priority sector lending requirements of RBI continue to be the major drivers of securitisation volumes. In terms of asset classes, ABS forms the larger part of the securitisation volumes. However, in financial year 2012-2013, the volumes shrunk by 20% due to the uncertainty in the market on the tax front.

Key investors in the market:

The key investors in the securitisation instruments are largely as follows:

a. Banks/ Financial Institutions/ NBFCs
b. Mutual Funds
c. Insurance Companies

In India the key motivations to invest in securitized paper have been meeting the priority sector lending requirements, capital relief and liquidity. However, the motivations to invest in securitized paper for various investor segment is myriad. The investors in the market are currently very centric and there is a need for broad basing the investors so that the motivation for securitisation is not restricted to meeting the priority sector lending requirements for banks alone.

Motivations for investments in securitised paper:

Securitised paper is typically highly rated (typically can reach AAA rating as well), fully secured, yet provides good yields. The advantages of securitisation to the investors in general include the following:

- Better Security, as investors have a direct claim over a portfolio of assets;
- Investment in rated structured finance products;
- Rating Resilience, as securitisation investment is considered safer than corporate debt;
- Flexible Instruments to serve various investment objectives;
- Diversification in investment portfolio;
- Fixed income security, availability of medium term and long term instrument.

Investment Regulations on FIIs:

RBI regulations for investments by FIIs

Investment norms for Foreign Institutional Investors are laid down in Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000[4] ("**Regulation**"). Regulation 5(4) states that –

> *"(4) A non-resident Indian or a registered FII or a Foreign Central Bank or a QFI or any other person resident outside India included in Schedule 5 may purchase securities, other than shares or convertible debentures of an Indian company, subject to the terms and conditions specified in Schedule 5"*

Further Schedule 5 to the Regulation lists down such securities (other than equity and convertible debt) in which registered FIIs can invest. The schedule permits certain securities

[4] http://rbi.org.in/Scripts/NotificationUser.aspx?Id=174&Mode=0

that a registered FII may purchase on repatriation basis either directly from the issuer of such securities or through a registered stock broker on a recognized Stock Exchange in India subject to the terms and conditions as specified by the SEBI and the Reserve Bank from time to time:

a. dated Government securities/treasury bills
b. listed non-convertible debentures/bonds issued by an Indian company
c. commercial papers issued by an Indian company
d. units of domestic mutual funds
e. Security Receipts issued by Asset Reconstruction Companies
f. Perpetual Debt instruments eligible for inclusion as Tier I capital and Debt capital instruments as upper Tier II capital issued by banks in India
g. listed and unlisted non-convertible debentures/bonds issued by an Indian company in the infrastructure sector
h. non-convertible debentures/bonds issued by Non-Banking Finance Companies categorized as 'Infrastructure Finance Companies'
i. Rupee denominated bonds/units issued by Infrastructure Debt Funds

SEBI regulations for investments by FIIs:

Section 2(f) of the Securities Exchange Board of India (Foreign Institutional Investors) Regulations, 1995[5] defines Foreign Institutional Investors (FIIs) to mean --

> *"Foreign Institutional Investor" means an institution established or incorporated outside India which proposes to make investment in India in securities;"*

Regulation 15(1) of the Regulation provides for investment restrictions on FIIs and the list of permitted investments include:

a) securities in the primary and secondary markets including shares, debentures and warrants of companies unlisted, listed or to be listed on a recognised stock exchange in India; and
b) units of schemes floated by domestic mutual funds including Unit Trust of India, whether listed on a recognised stock exchange or not, [units of scheme floated by a Collective Investment Scheme.]
c) dated Government Securities;
d) derivatives traded on a recognised stock exchange;
e) commercial paper;
f) security receipts;

SEBI FPI Regulations:

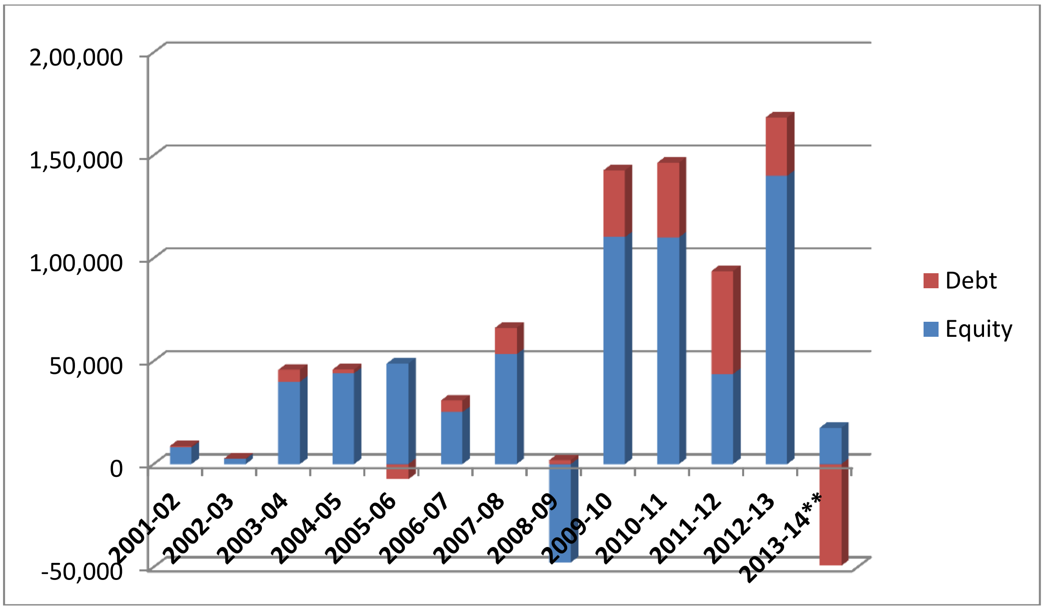
With the intent of integrating policies for foreign investments, SEBI vide Press Release (*PR No. 99/2013*) on 5th October, 2013 conveyed the approval of draft FPI Regulations. Under Chapter II of the FPI Regulations, FIIs or the sub-accounts who have been granted registration by the Board shall be deemed to be foreign portfolio investors for the purpose of these regulations.

[5] http://www.sebi.gov.in/acts/fiiregu2009.pdf

Further, Regulation 22 of the draft FPI Regulations lays down investment restrictions which include:

> a) *Securities in the primary and secondary markets including shares, debentures and warrants of companies, listed or to be listed on a recognized stock exchange in India;*
> b) *Units of schemes floated by domestic mutual funds, whether listed on a recognized stock exchange or not;*
> c) *Units of schemes floated by a Collective Investment Scheme;*
> d) *Derivatives traded on a recognized stock exchange;*
> e) *Treasury Bills and dated Government Securities;*
> f) *Commercial Papers issued by an Indian company;*
> **g) *Security Receipts issued by Asset Reconstruction Companies;***
>
> ….
>
> ***(m)Such other instruments specified by the Board from time to time.(emphasis ours)***

FIIs have estimated invested Rs. 13,000 crores in the Indian stock market in September, 2013 and since the beginning of 2013 have infused Rs. 73,398 crores in equities and have withdrawn Rs. 36,914 crores from the debt market. FIIs are a huge channel for attracting dollar inflows in the system. Over the years, FIIs have been consistently investing in equity and debt securities (except for 2008-09 which can be explained to be impacted by the financial crisis and in 2013-14 till date due to several macro-economic factors impacting the country) in the Indian system as is reflective from the data below:



Source: http://www.sebi.gov.in/cms/sebi_data/commondocs/FIIInvestmentFY_h.html
**Data available till 30th September, 2013