Citi delivers innovations in the Agency and Trust business

The Agency & Trust business is becoming more dynamic in line with the growth of the region’s capital markets and the introduction of new transaction structures. Issuers, Investors and Financial Advisers are becoming more demanding and are looking for a service provider such as Citi to deliver the “plumbing” that is so crucial for every type of capital markets transaction. Ben Lumley-Smith, director and Asia Pacific region head for Issuer Services at Citi’s Securities and Fund Services, discusses how the bank is responding to these needs.

The corporate trust and agency business in the region seems to be doing very well. What explains this trend?

Asian markets have certainly become stronger since the Asian financial crisis. A lot of liquidity is being pooled in the region and global and domestic bonds out of Asia have become very popular among investors across the globe.

The region has also benefited from the considerable changes effected in the past ten years, not only in the variety of instruments coming to market but also in terms of regulatory sophistication in markets. China and Taiwan, for example, recently promulgated securitization laws to help promote specific financing tools. Japan passed new laws to allow additional asset types to be securitized as well as updating its trust laws.

What differentiates Citi from the competition in offering these services?

With a well-established franchise in global transaction services – in cash management, securities and fund services, and trade – Citi already has the bricks and mortar in place in all growing markets around the world. We have an equally strong presence in investment banking, commercial banking and consumer banking. We are a significant player in the issuer service side of the business encompassing depositary receipts and the agency and trust business where our franchise is thriving in both the debt and equity spectrums. We have become a one-stop shop, protecting investors when it comes to bond issuance and different types of capital markets transactions. A key differentiator from our competition is the fact that we service not only global and Euro cross-border transactions, but we are also very active in many of the local markets here in Asia. The broad platform capability combined with a team of seasoned professionals with over 10 years experience each in Asia is a key element to Citi’s success.

What services does Citi provide?

Citi’s Agency and Trust business provides a range of agency, fiduciary, tender and exchange and depositary and escrow services globally. Essentially, we provide the “plumbing” for all types of capital markets transactions, such as debt and equity linked capital markets issuances, structured and project finance and bond/debt restructurings by offering needed services including:

- Trustee - Note, Bond or Indenture Trustee
- Security Trustee/Agent
- Calculation Agent
- Foreign Exchange Agent
- Security Custodian
- Conversion Agent
- Tax Withholding Agent
- Registrar
- Common depositary for the European based clearing systems
- Transaction administrator for securitization transactions
- Back-up servicer for certain securitization transactions

Who do you work with in deals?

We target our services to corporate issuers, the investment banking community as we are a common carrier, as well as major law and accounting firms, rating agencies and specialized credit enhancers to help them bring highly complex transactions to the market.

What exactly is Citi’s role in this business?

Our goal is to proactively and judiciously support clients wherever their financial adviser/investment bank takes them depending on prevailing market conditions and the client’s own needs. This is important given that each market in the region has very different legal and regulatory environments. We ensure, for instance, that the interests of the investors are protected in case of defaults or non payments of principal &/or interest. We do this by poring over the details of the transaction and the deal documentation to ensure that the deal works mechanically for the life of the transaction which can take multiple years. The bank always builds the best solution for the client no matter how complex the nature of the transaction, whether this is in debt issuance, debt exchange, structured finance, project finance, escrow and equity tender and exchange.

Citi is a natural choice for providing corporate trust and agency services given our extensive presence in local markets: its triple A credit rating, global footprint, brand recognition and reputation in the market.

Globally, we provide multiple agency and fiduciary services to more than 2,500 clients worldwide, ranging from governments and supra-national agencies to major corporations and other capital market participants.

How has the Agency and Trust business grown in the Asia-Pacific region in the last five years?

There has been considerable expansion of corporate trust activities in the region on the back of the increased liquidity in the market, the changing legal and regulatory environment as mentioned previously, changing investor appetite and a greater understanding of the types of products being issued into the equity and debt capital markets. At Citi we need to constantly be vigilant to...
the changes in the markets to ensure that as a service provider we can best support our clients.

A specific example of how far the markets have come would be to quote from the experience in Japan, when historically securitization transactions were structured through a twin Cayman SPC mechanism into the Euro markets and typically at a AAA level with a subpiece. Deals in that market today are now structured through an onshore Japanese trust mechanism and typically multi tranch for investors looking for higher yielding assets.

**How have warm back-up services for securitization transactions been received in Asia?**

Warm back-up servicing has been developed to add credit enhancement to securitization transactions and in line with Credit Rating Agency requirements on certain transactions and asset types. This is very important for off balance sheet structures where the investors do not have recourse to the originator (sometimes known as the “seller/servicer”) and have to rely on the performance of the underlying portfolio of assets.

For instance, should a mortgage originator issue a mortgaged backed securitization, the investors will not have recourse to that mortgage originator once there has been a default on the payment of either principal &/or interest on the bond. The investors’ only recourse will be to collect the value left in the underlying pool of receivables. The key question for the investors and rating agencies is what happens should the servicing entity not be able to continue servicing the securitized assets?

Back in the mid 1990s when the Asian securitization started to develop some momentum, the back-up servicing solution was very much on a “cold basis” – ie typically, the Note or Bond Trustee would sign up as cold back-up servicer on a “best efforts” basis. What this meant was that if the originator went into default the Note/Bond Trustee would try and find a replacement servicer with-in a stipulated timeframe but typically within 90 days.

As a team, we put together the first “warm” back-up servicing solution in Asia for a deal that was originated out of Indonesia. Basically, we step in and make sure that the portfolio data from the originator’s servicing platform can be read on the back-up servicer’s own servicing platform.

Typically, the rating agencies require a back-up servicer to be in the same industry as the originator with the same collection methodology so that if there is ever a default there is minimum downtime between transferring the latest data from the originator onto the back-up’s platform to allow servicing.

The “cold” solution was actually tested with the demise of JLC, a Japanese originator of ABS that went into default in 1998. The cold solution did not work and fortunately the trustee in bankruptcy allowed JLC to continue servicing those assets. As a direct result of JLC, we again brought in warm back-up servicing into that market. This standard was critical not only to the monoline insurers who were wrapping the securitized bonds (ie guaranteeing the principal and interest) of said bonds but also to investment banks who were providing warehouse finance. It also helped the Japanese securitization market re-start following the default of JLC.

**How do rating agencies value back-up servicing when it comes to assessing an issue?**

Each rating agency will have their own standard rating criteria depending on asset type, country of origin and a plethora of other key data points. They will run simulations on the securitized portfolio to stress test for performance and with which to assign a credit rating.

The results of the stress testing of the portfolio will help the rating agencies determine the requisite levels of enhancements including back-up servicing.

**Who selects the trustee and what are the key criteria for selection?**

This really depends on the sophistication of the originator of the bonds and whether they have an existing relationship with a Trustee provider. Other originators will rely on their investment bank to make that determination again in line with that institution’s experience in the market with the various trust providers. Typically, we are approached late on in the deal life cycle and is what we call the “five to midnight” scenario.

The quality and experience of the team is critical in these situations and can be a key element in not delaying a deal coming to market.

**What are your main countries of focus?**

We are growing our business across the Asia region. Certainly there are key themes and variations country by country but we are seeing increased volumes across the board. China and India have been very active in the pre-IPO convertible bonds and high yield space given their respective rising stock markets while Australia continues to be a robust market given the continued interest among investors for holding Aussie dollar denominated assets.

More recently, we have seen the first RMB bond issuance placed in Hong Kong by China Development Bank. We have hired experienced professionals in India, Bangladesh, Hong Kong and China. In Bangladesh, we are seeing a lot of activity in the telecoms/infrastructure space whilst in China, India and Australia we are actively involved in M&A activities through our account bank and escrow services.

**Can you talk about the importance of experience of the deal professionals?**

Citi’s Issuer Services team comprises 26 dedicated professionals based in Japan, Korea, Taiwan, China, Hong Kong, Bangladesh, India and Singapore and the team continues to grow. The Asia team complements a global team of some 200 plus in the front office with major locations being New York, Mexico and London.

The team at Citi is extremely experienced and well versed in the key documentation and settlement issues that come into play as capital markets transactions are issued. By having such expertise, we help the investment banks and their clients deliver transactions to market faster and more efficiently, thereby allowing the bankers to move onto their next deal. We however, do not walk away as we generally retain our roles for the life of the transaction which could be as long as 20 years.