

Non-Bank Financial Institutions

A three day intensive case study based workshop offering an overview of the credit analysis of securities companies (brokers and broker dealers), finance and leasing companies and investment funds and asset managers (funds and investment managers).

TARGET AUDIENCE

A case study based credit workshop designed for commercial, investment banking, fixed income, and regulatory and other risk professionals responsible for credit risk management, origination, investment, sales and trading, audit, regulation or underwriting. The workshop assumes a basic understanding of financial markets, products and accounting.

FitchTraining also offers more detailed counterparty specific workshops on Securities Companies, Funds and Fund Managers, Regulated Funds and Fund Managers, Hedge Funds and Central Counterparties, Clearing Houses and Exchanges. Some of these workshops have considerable overlap with this workshop.

COURSE OBJECTIVES

The overall goal of this case study based workshop is to give participants a structured approach to the credit analysis of different types of non bank financial institution.

Participants will be equipped to:

- Distinguish the key business risks, financial indicators and accounting issues by sector, business line, type of institution or fund structure
- Use market indicators, quantitative and qualitative analysis to identify strong and weak performers and detect early signals of changing credit quality
- Appreciate how economic, structural, competitive and regulatory issues impact strategy and financial health
- Dissect financial statements to uncover key credit issues and the impact of differing accounting policies
- Structure transactions to minimise credit and other risks.

CONTENT

MODULE I: SECURITIES COMPANIES

ANALYTIC OVERVIEW

Section aims: apply a structured approach to the credit analysis of securities companies and compare this with the perspectives of regulators, rating agencies and debt and equity investors.

- Perspective on securities companies: regulators, rating agencies, debt and equity investors
- Purpose payback model – key issues in debt and counterparty exposures to securities companies.

OPERATING ENVIRONMENT

- Section aims: understand the impact of macro competitive and regulatory issues on risk profile and strategy
- Securities markets: foreign exchange, equity, fixed income, futures and other derivatives, commodities, etc.
- *Exercise:* securities company risk analysis
- Regulation and supervision: focal points of international, regional and local regulation; compare and contrast key markets.

FINANCIAL FUNDAMENTALS

Section aims: benchmark key performance indicators of different types of securities companies in order to identify both strong and weak performers and recognise early warning signals of credit deterioration,

- Statement logic: matching business model to expected financial statements; key accounting policies on fair valuation; risk of

window dressing

- Performance risk: revenue sources, earnings volatility and cost control
- Business risk: risk profile of broking, trading underwriting, advisory, settlement and clearing
- Market risk/asset quality: modelling market risk, securities haircuts, fair value techniques (FASB 154) off balance sheet exposures
- Counterparty credit risk in brokerage and derivatives activities
- Financial risk: managing funding stability and liquidity risk
- Capital adequacy: regulatory and analytic tools to assess the strength of capital and the risks of leverage; net capital, working capital and core capital
- *Illustration case study:* regional broker
- Early warning signals: financial and non-financial indicators.

MANAGEMENT, FRANCHISE AND OWNERSHIP

Section aims: understand the key strategic, corporate governance and risk management challenges of securities companies.

- Differing business models: broker, broker dealer, wholesale, retail and internet based
- Strategy, risk management (VAR and other models)
- Corporate governance and key man issues (for smaller Cos.)
- *Exercise:* failed corporate governance
- Operational risk challenges
- Shareholders: quality of financial and business support
- *Case study:* lessons learned from a failed securities company.

MODULE II: FINANCE AND LEASING COMPANIES

ANALYTIC OVERVIEW

Section aims: apply the purpose payback model to understand the key credit issues of finance and leasing companies.

- Key credit issues with finance and leasing companies
- Purpose payback model: dependence of finance companies on debt markets and refinance; warehouse and borrowing base facilities and other structural issues.

OPERATING ENVIRONMENT

- Section aims: understand the impact of macro competitive and regulatory issues on risk profile and strategy
- Key risks and competitive issues by sub-sector: sales finance, direct finance, captive finance, equipment finance and leasing, credit cards and mortgages
- *Exercise:* distinguishing the business models of finance cos.
- Impact of minimal regulation and supervision: legal framework of secured lending.

FINANCIAL FUNDAMENTALS

Section aims: benchmark key performance indicators of different types of finance and leasing company in order to identify both strong and weak performers and recognise early warning signals of credit deterioration.

- Statement logic; accounting policies for income, receivables, delinquencies and leases (finance versus capital leases)
- Business risk: financial tools to assess quality of lease and loan book; reserve adequacy, owned vs. managed book; residual risk
- *Case study:* large regional finance and leasing company
- Funding risk: stability and variety of wholesale funding sources, gap management, availability of contingency funding, liquidity

and

- Securitization: benefits and risk of off balance sheet funding vehicles; residual risk, mortgage servicing rights and gain on sale accounting
- Capital adequacy: leverage and solvency benchmarks
- *Exercise:* capital standards for finance companies
- Performance risk: balancing risk and return; income stability and expense control
- Early warning signals: lessons learned from a failed finance Co.
- *Case study:* a finance company in financial distress.

MANAGEMENT, FRANCHISE AND OWNERSHIP

Section aims: evaluate the business model of different types of finance and leasing company to ensure they have adequate franchise value to succeed.

- Franchise: assessing the validity of the business model, residual marketing, processes and systems, strategy, etc.
- *Case study:* large international leasing company.

MODULE III: REGULATED FUNDS AND FUND MANAGERS

INDUSTRY OVERVIEW

Section aims: differentiate the key features and investment strategies of regulated funds.

Orientation

- Types of fund: pension funds; regulated mutual funds, managed accounts, closed ended funds and investment trusts, tracker and exchange traded funds (ETFs), fund of funds, master feeders, REITs etc.
- Structure and legal status of funds and managed accounts.

Investment strategies

- Investment strategies: risk profile of strategy, policies, practices and restrictions
- Traditional strategies: fixed income (money market, bond, municipals) equity and specialist funds; growth, value and balanced strategies; capital guaranteed structures
- Alternative investment strategies: use of derivatives and leverage; liability driven investment (LDI) strategies for pension funds.

ANALYTIC OVERVIEW

Section aims: apply the structured approach to analysis to fund transactions in order to recognise the key challenges of exposures to funds.

Structured approach to analysis

- Purpose of transaction and sources of payback: Who is the counterparty? What assets or derivatives are being financed? How will the transaction be settled or debt repaid at maturity?

Perspectives on analysis

- Information sources: prospectus, financial statements, portfolio statements.

RISK ANALYSIS

I. OPERATING ENVIRONMENT

Section aims: understand the macro competitive and regulatory drivers of performance, strategy and financial strength.

Macro and competitive drivers

- Sub-sectors of the industry: institutional, retail, wealth management
- Competitive drivers: sources of advantage

Regulation and supervision

- Regulation and supervision by region (focus depends on location of workshop)
- Mutual fund regulations: investment and leverage restrictions,

disclosure

- Pension fund regulation: funded status; investment limitations,
- Fund manager regulation; capital adequacy, licensing, business practices.

II. FINANCIAL FUNDAMENTALS

Section aims: benchmark key performance indicators of different types of finance and leasing company in order to identify both strong and weak performers and recognise early warning signals of credit deterioration.

- "S": Size: reviewing size, diversification and market position of fund
- "M": Market risk: volatility measures e.g. standard deviation, VaR
- "A": Asset quality: liquidity and valuation of assets, haircuts
- "L": Liquidity: redemption risk on open ended funds
- "L": Leverage: use of financial and derivative leverage; funded status for pension funds
- "P": Performance: bench marking performance – NAV measures, information and Sharpe ratios.

III. MANAGEMENT

Section aims: evaluate the roles and responsibilities of key parties to a fund with a focus on the fund manager.

Key parties

- Roles and responsibilities of various parties: manager, trustee, directors, administrator, custodian etc.

Due diligence fund manager

- Business structure: staff and organisation: experience levels; size, affiliation
- Independence and controls: affiliation; conflicts of interest
- Investment process: structure and implementation of portfolio management decision making
- Risk management: operational, market, credit and regulatory
- Communication: disclosure and client relationships.

Fund manager as counterparty

- Purpose payback: why do fund managers borrow and how do they service debt
- Risk profiles of different business models
- Financial analysis a) Performance measurement b) Cash-flow analysis c) Balance sheet strength
- Early warning signals of troubled credits.

STRUCTURE

Section aims: structure exposures in order to optimise risk reward

- Types of risk when dealing with funds - credit, market, operational, reputation
- Exposure profile - assessing the appropriateness of the structure in terms of amount, maturity etc.
- Ranking - establishing and maintaining a senior position
- Safeguards - documentation (e.g. ISDA) and collateral.

Learning Paths

