

# **Letter from the Editors**

Vol.9, Nos. 1-4, 2002

## **Have You Securitized Your Receivables Lately?**

### **I. Ford Motor Credit and Securitization**

Ford Motor Credit is the captive finance company of Ford Motor Inc. Its primary business is to supply Ford Motor affiliated dealers with capital which they in turn use to finance inventories of unsold vehicles and make loans and extend leases to their retail and corporate customers. Ford Motor Credit purchases the loans dealers make to their retail customers at the negotiated purchase price of the vehicle net of any trade in value and down payment received by the customer. These loans then compose Ford Motor Credit's retail loan portfolio. Ford Motor Credit extends revolving credits to their dealers. This is known as dealer floorplan financing and composes the wholesale segment of Ford Motor Credit's receivable portfolio. In addition Ford Motor Credit through its PRIMUS division offers wholesale financing to dealers of vehicles sold under the Jaguar, Land Rover, Aston Martin and Mazda brand vehicles and purchases loans extended by these dealers. Ford Motor Credit also offers credit through subsidiaries that specialize in dealing used cars and have a clientele that is considered high risk or "non-prime" credit. Ford Motor Credit also offers financial services to vehicle leasing companies and fleet purchasers. Financial services include underwriting auto insurance

Ford Credit has used securitization since 1988 to refinance portions of its wholesale and retail receivable portfolio. In addition to its term securitization programs through which it refinances dealer floorplan loans, retail installment loans and leases, Ford Credit sponsors a single seller asset backed commercial paper program called FCAR Owner Trust. FCAR issues commercial paper to fund purchases of asset backed securities from bankruptcy remote wholly owned special purpose subsidiaries of Ford Motor Credit and business trusts sponsored by Ford Motor Credit.

Ford Motor Credit recently established an asset-backed notes program—the "Motown Notes Program"—which is used to refinance interests in pools of wholesale receivables known as dealer floor plan loans. The Motown Notes are issued out of the securitization vehicle Ford Credit Floorplan Master Owner Trust A. Dealer floorplan loans

are revolving credits that automobile dealers take out to finance their inventory of unsold cars. The loans are collateralized by the dealer's inventory of unsold cars. Of \$65 billion of wholesale motor vehicle credit extended by finance companies at June 30<sup>th</sup>, 2000, 40% was securitized. (Survey of Finance Companies, 2000, Federal Reserve Bulletin, January 2002)

Ford Motor Credit through its European Banking subsidiary FCE Bank has established a \$5 billion European securitization program called Globaldrive. Globaldrive B.V. is a Dutch special purpose vehicle that makes secured loans to securitization vehicles established by subsidiaries of FCE Bank. Globaldrive finances these secured loans by issuing asset-backed notes. The loans are secured by the asset-backed securities issued by special purpose securitization vehicles established by FCE subsidiaries. Globaldrive may also purchase the asset-backed securities or receivable pools. Each series of notes issued by Globaldrive is secured by a separate pool of finance receivables or series of asset-backed securities. The asset-backed securities are issued by bankruptcy remote special purpose vehicles that have purchased the loans from the FCE subsidy that originated the credit. Globaldrive is a compartmentalized securitization vehicle so that the credit quality of one series is isolated from the credit quality of other series issued by Globaldrive B.V. Investors that purchase asset-backed securities issued by Globaldrive are exposing themselves to the risk of a single compartment. Their exposure may or may not be leveraged with respect to the credit risk of the securitized pool of receivables depending upon the position of the security in the series, i.e. subordinate, mezzanine or senior. Globaldrive offers FCE Bank an efficient and alternative outlet to the capital markets through which it can refinance its retail and wholesale portfolios of receivables. Since 1997 the Globaldrive Program has issued four series of asset-backed notes to refinance approximately Euro 2.5 billion of receivables.

In the autumn of 2003 Ford Motor Credit sold about \$3 billion of retail receivables directly to Bear Stearns Asset Backed Funding Inc. (the Depositor) an affiliate of Bear,

## Exhibit 1

### Funding Spreads Compared to 3-Year U.S. Treasury (basis points)

	2001				2000	1999
	31-Dec	30-Sep	30-Jun	31-Mar		
Unsecured debt funding	264	217	131	160	157	86
Securitized funding	99	87	91	85	93	70
Unsecured over (under) securitized	165	130	40	75	64	16

\*The spreads listed are indicative only and do not reflect specific trades.

Source: Ford Motor Credit Annual Report, Form 10-K for the Year Ending December 2001

## Exhibit 2

### A2 Rated Finance Paper Spread Over Two Year Treasury Strip (basis points)

10/4/02	108 bp
10/4/01	102 bp
10/4/00	95 bp
10/4/99	88 bp
10/2/98	71 bp
10/3/97	38 bp
10/2/96	41 bp

Source: Bloomberg L.P

Stearns & Co. Inc. Bear Stearns Asset Backed Funding Inc. pooled a portion of the receivables purchased from Ford Motor Credit with portfolios of receivables purchased from Daimlerchrysler Services North America LLC and Volvo Finance North America Inc and securitized the receivables through a Qualifying Special Purchase Vehicle, Whole Auto Loan Trust 2002-1. Ford is using sales of receivables to further diversify its sources of liquidity and to protect itself from a premium that the markets may charge in the future for asset-backed securities issued by Ford sponsored trusts. Sources of this premium might be saturation of the market for securities coming out of the Ford programs or a perception in the market that stresses on Ford's balance sheet would filter through to asset-backed securities issued by Ford securitization programs. Even though these perceptions would be ignoring the fundamental strength of asset-backed securities—isolation and separation of receivable risk from transferor risk—it is perception that drives prices in the short run and liquidity problems can often become critical in the short run. Combining receivable pools from different originators into a single issue, Bear, Stearns is internalizing the diversifica-

tion process for investors and offering the originators a new path to the securitization markets.

Securitization has gone from being a marginal funding source for the captive finance companies of automobile manufactures to becoming one of their core sources of liquidity. Securitization is used to tap the capital and money markets on the stability and predictability of transparent pools of receivables numbering in the hundreds of thousands for transactions launched by the large captive finance companies of automobile manufacturers. While a company like Ford Motor Credit must pay rates corresponding to a BBB/P-2 (Standard and Poor's) corporate credit risk when issuing senior unsecured debt from its balance sheet, securitization offers Ford Motor Credit a way of refinancing a portfolio of receivables at a rate that is an average of AAA/BBB/BB/P-1 rated debt and a cost corresponding to Ford Motor Credit's cost of capital. Factoring in Ford Motor Credit's capital cost is necessary to account for the residual interest in the asset pool that is retained by Ford Motor Credit. The advantage of securitization increases as this average diminishes but even should the average equal a cost of BBB debt, securitization still offers advantages.

### Exhibit 3

Ford Motor Credit Inc.  
Securitized Funding as a per cent of Total Debt

	2001	2000	1999	1998	1997
Total Securitized Funding (billions of dollars)	\$46.2	\$24.7	\$16.0	\$12.2	\$9.0
Total Balance Sheet Debt	\$146.3	\$146.3	\$133.1	\$115.0	\$100.7
Total Securitized Funding as a Percent of Total Balance Sheet Debt	31.5%	16.8%	12.02	10.60%	8.9%

Source: Ford Motor Credit Annual Report, Form 10-K for the Year Ending December 2001

Securitization alleviates balance sheet pressures caused by excessive leverage ratios, low asset performance ratios or strained credit agreements.

Exhibit 1 shows the cost of refinancing receivables via securitization relative to the cost of funding the receivables with debt issued from Ford Motor Credit's own balance sheet. The advantage of securitized funding has increased as the credit rating of Ford Motor Credit has declined from A+ at 12/13/99 to BBB at 10/25/02 by Moody's Investors Service. In January of 2002 Moody's lowered Ford Motor Credit's short term credit rating from P-1 to P-2.

As FMCC's specific cost of funds has increased due to a deterioration in its balance sheet the general level of credit spreads has also increased. Exhibit 2 illustrates the yield spread between A2 rated paper issued by finance companies over the treasury strip curve. In response the decline in its own credit quality and the overall increase in credit spreads FMCC has de-emphasized its reliance on the corporate debt markets to the securitization markets. Exhibit 3 shows the extent of this shift in funding from on-balance sheet obligations to off-balance sheet transactions.

Ford Motor Credit explicitly states how securitization fits into their overall funding program. Ford's manage-

ment values the stability that securitization has offered as other sources of funds have become more costly and more uncertain. Companies that have relied too heavily on securitization have been squeezed and experienced severe liquidity problems when the market for subordinate tranches of asset-backed securities have become inaccessible.

"Maintaining liquidity through access to diversified sources of funds has always been a key factor in our funding strategy. We define liquidity as our ability to meet our funding needs, which includes purchasing retail installment sale and lease contracts, funding other financing programs and repayment of our debt obligations as they become due. In December 1988, we began selling a portion of our receivables in securitization transactions to fund our operations, and we have been a regular participant in the securitization market since then. Securitization represents an additional source of funding that has been less susceptible to changing market conditions." (Ford Motor Credit Annual report on Form 10-K for the year ended December 31, 2001).

**Charles A. Stone, *Université Paris Dauphine***  
**Anne Zissu, *Temple University***