ABSTRACT

Following the Monetary Authority of Singapore (MAS) directions to broaden and deepen Singapore’s capital markets, the property market has responded with the first Asset-Backed Securitisation (ABS) in Singapore. This breakthrough was achieved in 1999, when Neptune Orient Lines (NOL) sold its headquarter building at Alexandra Road for $185 million through ABS, achieving yet another milestone in Singapore’s fixed-income capital market. Following the NOL deal, eight other asset-backed securitisation deals have taken place between 1999 and 2001, which collectively siphoned a massive $3.05 billion of funds from the capital market. These are indicators of a growing significance of ABS as an alternative financing method. The originator in a typical ABS deal is basically seen as swapping the securitised property’s variable rental cash flows for fixed coupon interest payments under the bonds issued. The decision to enter into an ABS deal can be conceptually represented as a “swaption”. Based on the swap option pricing model developed by Fisher Black (1976), this paper seeks to quantify the effective cost of financing through ABS. The estimated financing cost by ABS was found to be significantly lower when compared with the cost of raising funds through traditional Fixed Rate Mortgage (FRM). The estimated securitisation cost of 268 Orchard Road was found to be approximately 7.6% of the bond value of $184 million. Sensitivity analyses were carried out to test the influence of different input factors: namely the 1) “swap start (years)”; 2) swap rate and 3) volatility of swap rate, on the cost of securitisation. Implications of the results were then discussed. Finally, other benefits of ABS to both the originator and investors were also examined.

Key Words:
asset-backed securitisation, swap option, cost of securitisation