WHITEPAPER

# Securitization Economics: A Quantitative Framework

Modeling expected proceeds, cost of issuance, and break-even analysis for your first ABS transaction.


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# Contents

# Executive Summary

Securitization transforms illiquid loan portfolios into tradeable securities, unlocking capital efficiency and lower funding costs. But the decision to securitize — and the structuring of any given deal — is fundamentally an economic exercise. Understanding the quantitative framework behind securitization economics is essential for every emerging lender evaluating capital markets access.

This whitepaper provides a practitioner-level framework for modeling securitization economics — from estimating gross proceeds and all-in costs to building break-even analyses that inform your go/no-go decision. Whether you are evaluating your first transaction or optimizing a repeat issuance program, this guide equips you with the tools to make data-driven capital markets decisions.

| 95-98% | 1-3% | 100-300bp |
|---|---|---|
| TYPICAL GROSS PROCEEDS | ALL-IN ISSUANCE COST | SPREAD SAVINGS VS. WAREHOUSE |

**KEY TAKEAWAYS**

- Gross proceeds from a well-structured ABS deal typically range from 95-98% of collateral balance.
- All-in issuance costs for inaugural deals run 1-3% of deal size, declining 30-50% for subsequent deals.
- Break-even portfolio size is typically $150-250M in annual originations for consumer lending.
- The economics improve dramatically with each subsequent issuance as fixed costs amortize and spreads tighten.

CHAPTER 1

# The Economics of Securitization

## Why Securitize? The Economic Case

The fundamental economic proposition of securitization is straightforward: by converting loans into rated securities backed by asset cash flows — rather than your corporate credit — you access a deeper, more diverse pool of capital at lower cost. The magnitude of this benefit depends on the spread differential between your warehouse funding cost and the blended ABS coupon, net of issuance expenses.

For a typical consumer lending platform with warehouse funding at SOFR + 300-400 bps, a well-executed ABS transaction can achieve a blended all-in cost of SOFR + 150-250 bps — a savings of 100-200+ basis points. On a $200M deal, this translates to $2-4M in annual interest savings.

## The Economic Building Blocks

Securitization economics can be decomposed into four key components that together determine whether a deal creates value:

1. Gross proceeds: The total cash raised from selling bonds to investors, determined by tranche sizes, advance rates, and pricing.
2. Cost of issuance: One-time expenses including legal, rating agency, underwriting, and structuring fees.
3. Ongoing cost of carry: The blended coupon paid to bondholders plus servicing, trustee, and administrative expenses.
4. Residual economics: Excess spread, overcollateralization build, and residual cash flows returned to the originator.


## Key Economic Metrics

| METRIC | DEFINITION | TYPICAL RANGE |
|---|---|---|
| Gross Proceeds | Total bond sales as % of collateral | 95-98% |
| Advance Rate | Senior + mezz bonds as % of pool | 85-95% |
| Weighted Avg. Coupon | Blended rate paid to all bondholders | SOFR + 130-220 bps |
| Excess Spread | Collateral yield minus bond coupon and fees | 200-500 bps |
| Cost of Issuance | One-time deal costs as % of deal size | 1.0-3.0% |
| Residual Return | Equity holder IRR on retained tranche | 12-25%+ |

CHAPTER 2

# Revenue Drivers: Modeling Proceeds

## Capital Structure and Tranching

The gross proceeds of a securitization are determined by the capital structure — specifically, the total par value of bonds sold to investors. A typical ABS deal is divided into multiple tranches, each with a different rating, coupon, and size.

| TRANCHE | RATING | TYPICAL SIZE | SPREAD (SOFR+) | COUPON |
|---|---|---|---|---|
| Class A | AAA | 78–85% | 80–150 bps | SOFR + 100–150 bps |
| Class B | AA | 5–8% | 150–250 bps | SOFR + 175–225 bps |
| Class C | A | 3–5% | 225–375 bps | SOFR + 275–350 bps |
| Class D | BBB | 2–4% | 375–550 bps | SOFR + 400–500 bps |
| Equity | NR | 5–12% | N/A | Residual cash flow |

Illustrative capital structure for a consumer unsecured ABS deal.

The sum of all rated tranches (Class A through D in this example) represents the gross bond proceeds — typically 88–95% of the collateral balance. The equity tranche is retained by the originator and represents your first-loss position and alignment of interests with bondholders.

## Factors That Affect Proceeds

- Credit quality of the collateral: Higher credit quality allows for thinner subordination (larger senior tranche) and tighter spreads.
- Performance track record: Issuers with multiple successful deals achieve higher advance rates and lower credit enhancement.
- Asset class precedent: Asset classes with deep ABS histories (auto, credit card) command tighter pricing than newer sectors.
- Market conditions: Tight credit markets widen spreads and may reduce demand for lower-rated tranches.
-

Deal structure: Revolving vs. static pool, excess spread trapping, and trigger mechanics all affect investor perception.

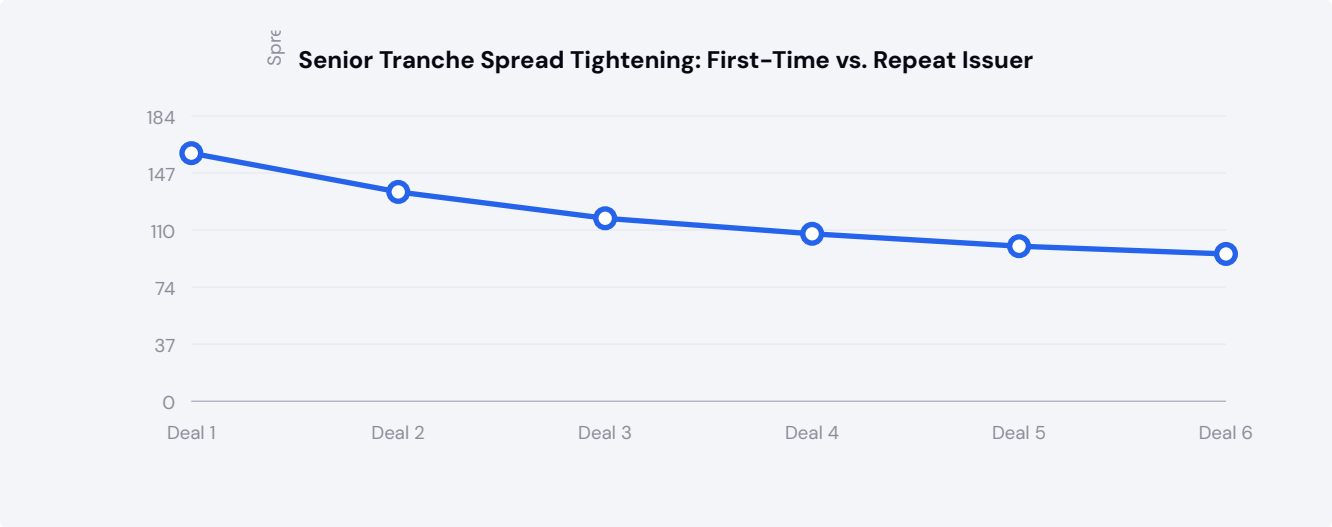
## Estimating Gross Proceeds

For a $200M collateral pool with a 90% advance rate across rated tranches:

- Rated bonds issued: $180M (90% of $200M)
- Retained equity: $20M (10% of $200M)
- Gross bond proceeds: $180M (before issuance costs)
- Net proceeds: $175.5M (after ~$4.5M in estimated issuance costs)
- Funding improvement: $175.5M in long-term, locked-rate financing vs. $170M from warehouse at 85% advance

## Pricing Dynamics

Bond pricing is the product of negotiation between the arranger and investors during the bookbuilding process. The arranger markets the deal at initial price talk (IPT) — a preliminary spread range — and tightens or widens based on investor demand.




As this chart illustrates, senior tranche spreads typically tighten by 40-60 bps between an inaugural deal and the fourth or fifth issuance. This spread compression, combined with declining issuance costs, creates a powerful economic incentive for building a programmatic ABS platform.

## The Weighted Average Coupon

The weighted average coupon (WAC) is the blended interest rate you pay across all tranches. For the illustrative capital structure above:

| TRANCHE | SIZE | COUPON | WEIGHTED CONTRIBUTION |
|---|---|---|---|
| Class A (82%) | $164M | SOFR + 120 bps | 98.4 bps |
| Class B (6%) | $12M | SOFR + 200 bps | 12.0 bps |
| Class C (4%) | $8M | SOFR + 300 bps | 12.0 bps |
| Class D (3%) | $6M | SOFR + 450 bps | 13.5 bps |
| Blended WAC | $190M | SOFR + 136 bps | 135.9 bps |

Blended WAC of SOFR + ~136 bps vs. warehouse cost of SOFR + 300+ bps.

### THE PROCEED-SPREAD TRADEOFF

Higher advance rates (more bonds sold) increase proceeds but also increase the blended coupon — because the incremental bonds are lower-rated and higher-spread. The optimal capital structure balances maximum proceeds against minimum blended cost. Your arranger will help you find this balance.

CHAPTER 3

# Cost of Issuance

## One-Time Deal Costs

Issuance costs are the upfront expenses incurred to structure, rate, and execute a securitization. These costs are highest for inaugural deals and decline significantly for subsequent transactions as legal templates exist, rating agency models are established, and processes are streamlined.

| COST CATEGORY | INAUGURAL DEAL | REPEAT DEAL | NOTES |
|---|---|---|---|
| Underwriting fee | $1.0-2.0M | $0.6-1.2M | 50-100 bps of deal size; declines with repeat |
| Legal (issuer) | $500K-1.0M | $200-400K | Template reuse reduces repeat deal cost |
| Legal (underwriter) | $300-500K | $150-300K | Standardized docs reduce effort |
| Rating agencies | $200-500K | $150-300K | Per-agency fee; surveillance is ongoing |
| Accounting/audit | $75-150K | $50-100K | True sale opinion, comfort letters |
| Trustee/admin | $50-100K | $40-75K | Setup plus first-year fees |
| Printing/filing | $25-75K | $20-50K | Offering documents, SEC filings |
| Other | $50-100K | $25-75K | Road show, data room, misc. |

Ranges reflect a $200M consumer loan ABS deal. Costs scale with deal size and complexity.

**$2.2-4.4M**
INAUGURAL DEAL COSTS

**$1.2-2.5M**
REPEAT DEAL COSTS

**40-50%**
COST REDUCTION BY DEAL 3

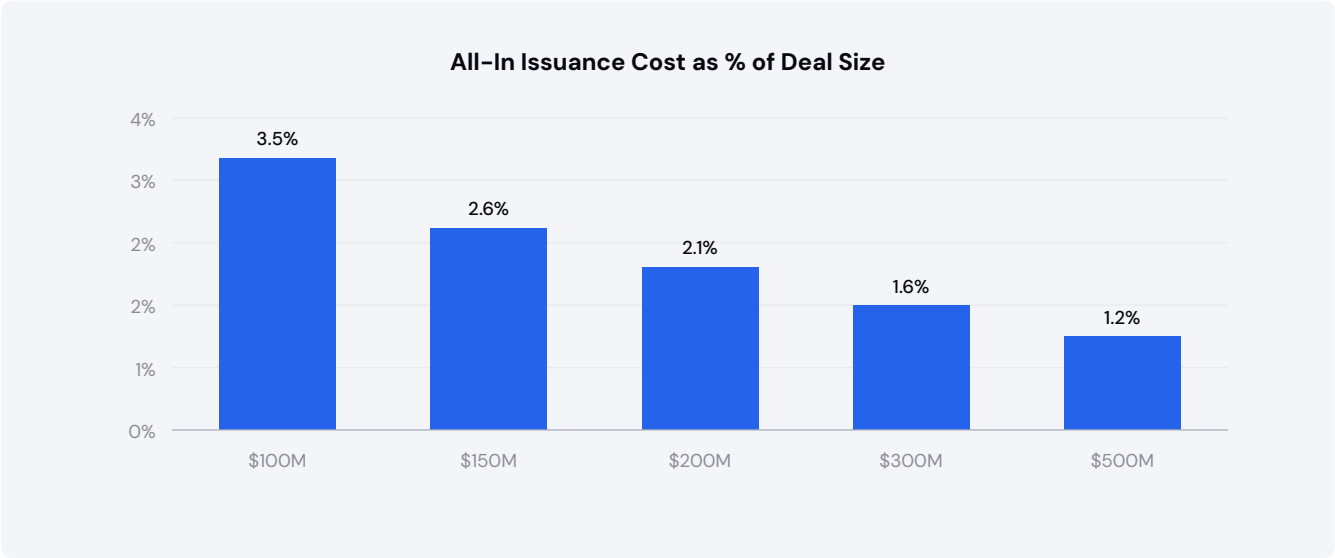
## Ongoing Costs

Beyond one-time issuance costs, ABS transactions carry ongoing expenses throughout the life of the deal:

- Servicing fee: 25-100 bps annually, paid from collections (typically to the originator as servicer).
- Trustee/administration fee: $30-75K annually for the indenture trustee and paying agent.
- Rating agency surveillance: $25-75K per agency annually for ongoing monitoring.
- Accounting and compliance: $25-50K annually for ongoing reporting, 10-D/10-K filings (if public).
- Backup servicer: $10-25K annually in standby fees.

## Cost Amortization and Scale Effects

Many issuance costs are largely fixed — they don't scale linearly with deal size. This creates powerful economies of scale. A $100M deal and a $300M deal may have similar legal and rating agency costs, but the per-dollar cost drops dramatically for the larger transaction.




### THE REPEAT ISSUANCE ADVANTAGE

The economic case for building a programmatic ABS platform is compelling. By your third deal, issuance costs typically decline 40-50%, spreads tighten 30-50 bps, and execution timelines compress from 12-16 weeks to 6-8 weeks. The cumulative effect can double the net economic benefit of securitization relative to your inaugural transaction.

CHAPTER 4

# Credit Enhancement Economics

## What Is Credit Enhancement?

Credit enhancement (CE) is the structural protection built into an ABS deal that shields senior investors from losses. The level of CE required for each rating level is determined by rating agency models based on your collateral's expected loss profile. CE is the primary driver of your deal's capital structure — and therefore your economics.

## Forms of Credit Enhancement

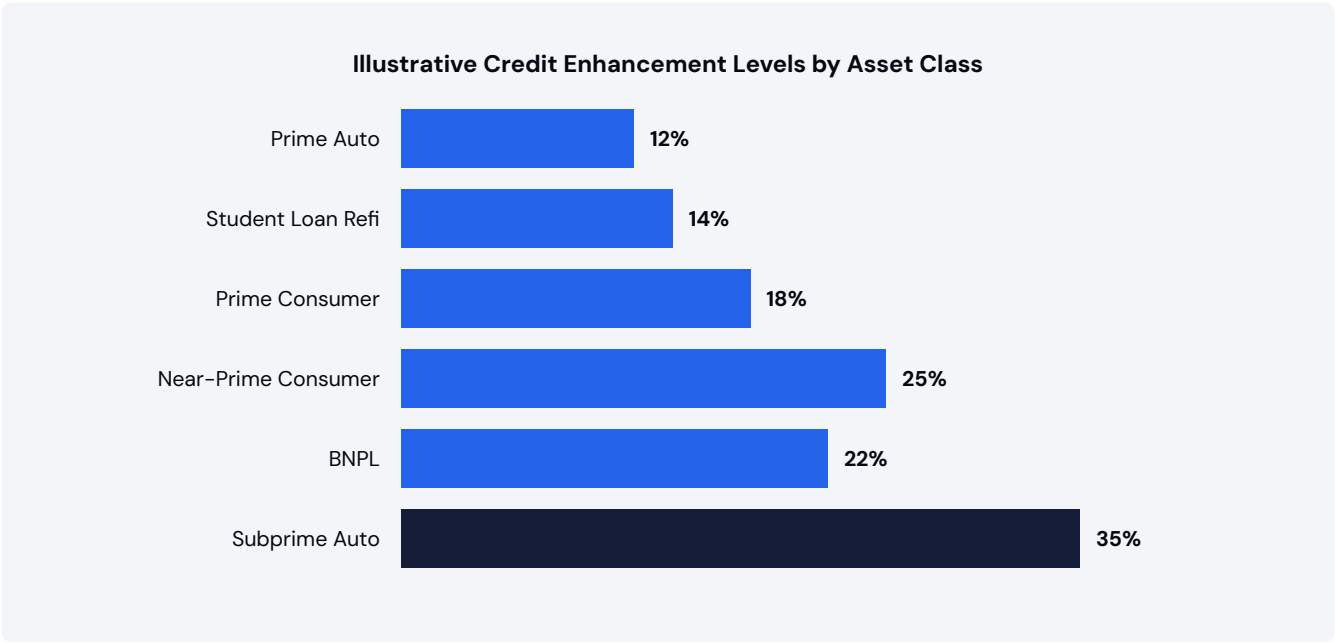
| CE TYPE | MECHANISM | ECONOMIC IMPACT |
|---|---|---|
| Subordination | Junior tranches absorb losses before senior | Reduces senior size, increases blended cost |
| Overcollateralization | Pool balance exceeds bond balance | Reduces net proceeds below par |
| Excess spread | Loan yield exceeds bond coupon + fees | Traps cash flow; builds OC over time |
| Reserve account | Cash funded at closing for shortfalls | Reduces day-one proceeds |

## How Rating Agencies Determine CE Levels

Rating agencies use proprietary models to simulate loan pool performance under stress scenarios. The CE required for each rating level is the amount needed to cover projected losses at that stress level with a high degree of confidence.

- AAA CE: Must withstand losses 3-5x the base case expected loss rate.
- AA CE: Must withstand losses 2.5-4x the base case.
- A CE: Must withstand losses 2-3x the base case.
- BBB CE: Must withstand losses 1.5-2.5x the base case.

For a consumer loan pool with a 5% base-case expected loss, AAA CE might be set at 18-25%, meaning the senior tranche has 18-25% of the capital structure protecting it from losses. This directly determines the maximum size of your AAA tranche — and therefore your blended cost of funds.



## The CE-Proceeds Tradeoff

Higher CE means lower credit risk for investors (and therefore tighter spreads on senior tranches), but it also means a smaller senior tranche and lower gross proceeds. The optimal balance depends on your asset quality, the specific rating agency models, and market conditions.

Over time, as your performance track record demonstrates lower-than-modeled losses, rating agencies may reduce CE requirements for subsequent deals. A 2-3% reduction in AAA CE translates directly to 2-3% more bonds sold at the tightest spread — a meaningful economic improvement.

## Excess Spread as Dynamic CE

Excess spread — the difference between the yield on your loan pool and the blended coupon paid to bondholders, net of fees — serves as a first line of defense against losses. Each month, excess spread flows through the waterfall and can be used to cover losses before they impact any tranche. A pool with 6% gross yield and a 2% blended bond coupon generates approximately 4% in annual excess spread (before fees), providing substantial loss absorption capacity.

Rating agencies give partial credit for excess spread in their models, which reduces the hard CE requirement. A deal with high excess spread can achieve the same rating with lower subordination — improving your proceeds.

> **OPTIMIZING CE LEVELS**
>
> Work with your arranger and rating agencies early to understand the CE dynamics for your specific collateral. Providing granular, high-quality data allows agencies to build more precise models — and more precise models typically result in lower CE requirements than conservative default assumptions. This is one of the most direct ways that data quality translates into economic value.

CHAPTER 5

# Cash Flow Modeling

## The Cash Flow Waterfall

The payment waterfall defines how cash collected from the loan pool is distributed each period. Understanding the waterfall is essential for modeling your economics as the equity holder — because your residual return depends on what's left after all other obligations are met.

1. Trustee fees and deal expenses (typically small fixed amounts).
2. Servicing fee (25–100 bps of outstanding pool balance).
3. Senior tranche interest (Class A coupon).
4. Senior tranche principal (amortization or target balance).
5. Mezzanine tranche interest and principal (Class B, C, etc.).
6. Replenishment of reserve account and OC target.
7. Subordinate tranche interest and principal.
8. Residual to equity holder (originator).

## Modeling Monthly Cash Flows

A robust cash flow model projects monthly collections, losses, prepayments, and the waterfall distribution over the life of the deal. Key assumptions include:

| ASSUMPTION | BASE CASE | STRESS CASE | SOURCE |
|---|---|---|---|
| Gross default rate | 5.0% ann. | 12.5% ann. | Static pool vintage analysis |
| Recovery rate | 15% | 8% | Historical recovery data |
| Prepayment speed | 18% CPR | 12% CPR | Historical prepayment curves |
| Delinquency rate | 3.5% (60+) | 8.0% (60+) | Historical delinquency data |
| Loss timing curve | 24-mo peak | 18-mo peak | Vintage loss curve analysis |

Illustrative assumptions for a consumer unsecured loan ABS deal.

## Residual Cash Flow to the Originator

As the equity holder, your return comes from excess spread and residual cash flow after all bond obligations are met. In a well-performing deal, the equity tranche can generate IRRs of 12-25%+ — making the retained first-loss position a meaningful source of economic value, not just a regulatory requirement.

## Sensitivity Analysis

Your cash flow model should test sensitivity to key variables. Small changes in loss rates, prepayment speeds, and recovery rates can meaningfully impact equity returns and deal economics.

| SCENARIO | NET LOSS | EQUITY IRR | SENIOR TRANCHE IMPACT |
|---|---|---|---|
| Base case | 4.3% | 22% | None — full repayment |
| Moderate stress | 7.5% | 14% | None — CE absorbs losses |
| Severe stress | 11.0% | 4% | None — CE absorbs losses |
| Extreme stress | 16.0% | -8% | Mezzanine impacted; senior protected |

Illustrative sensitivity analysis showing equity returns under various loss scenarios.

## Duration and Reinvestment

The weighted average life (WAL) of your ABS bonds determines how long your capital is deployed at ABS rates versus warehouse rates. Shorter WAL means you get capital back sooner and can reinvest into new originations — but it also means the spread savings are captured over a shorter period. For most consumer lending ABS, WAL is 1.5-3 years, which provides a good balance between funding duration and capital recycling.

### MODEL BEFORE YOU COMMIT

Build your cash flow model before engaging an arranger. A well-constructed model gives you the analytical foundation to evaluate term sheets, negotiate structure, and make informed decisions throughout the deal process. Don't rely solely on your arranger's model — maintain your own independent view of economics.

CHAPTER 6

# Break-Even Analysis

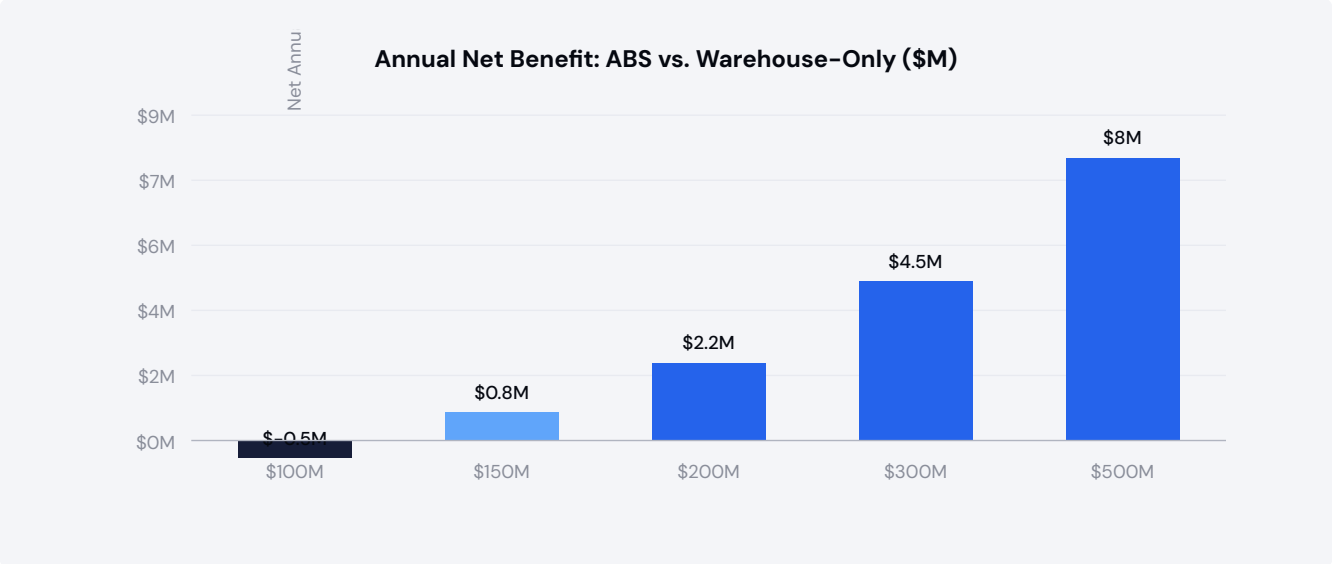
## When Does ABS Make Economic Sense?

The break-even analysis compares the all-in cost of ABS funding against your current warehouse cost to determine the minimum portfolio scale and deal frequency at which securitization creates net value. The analysis must account for both the ongoing spread savings and the upfront issuance costs.

### The Break-Even Formula

Net ABS benefit = (Warehouse spread - ABS blended spread) x Average outstanding balance x Time - Issuance costs

For securitization to create value, the cumulative spread savings over the life of the deal must exceed the issuance costs. Given typical issuance costs of $2-4M for an inaugural deal and spread savings of 100-200 bps, the break-even generally occurs at:




## Break-Even by Deal Frequency

The economics also depend on how frequently you issue. More frequent issuance means you spend more time funded at ABS rates rather than warehouse rates. For a lender originating $300M annually:

| ISSUANCE FREQUENCY | AVG. ABS FUNDED | ANNUAL SPREAD SAVINGS | NET OF COSTS |
|---|---|---|---|
| Annual (1x) | 50% of portfolio | $2.3M | $0.8M |
| Semi-annual (2x) | 70% of portfolio | $3.2M | $1.7M |
| Quarterly (4x) | 85% of portfolio | $3.9M | $2.4M |

Assumes 150 bps spread savings, $200M average outstanding, $1.5M per-deal cost for repeat issuance.

CHAPTER 7

# Scenario Analysis and Stress Testing

## Building Scenario Models

Robust economic analysis requires modeling multiple scenarios — not just the base case. Your model should capture how deal economics change under different market conditions, credit environments, and structural assumptions.

### Key Scenarios to Model

- Base case: Expected performance based on historical data and current credit environment.
- Spread widening: What if market spreads widen 50-100 bps from pricing expectations?
- Credit deterioration: What if portfolio losses increase 50-100% from base expectations?
- Prepayment acceleration: What if prepayment speeds increase, shortening WAL and reducing excess spread?
- Rate environment change: What if SOFR moves +/- 200 bps?
- Delayed issuance: What if you need to wait 3-6 months for a better market window?

## Stress Testing Your Capital Plan

Beyond individual deal economics, stress-test your overall capital plan. What happens if you can't access the ABS market for 6-12 months due to market disruption? Do you have sufficient warehouse capacity to continue originating? What is the cost of carrying loans on the warehouse for an extended period?

| SCENARIO | IMPACT ON ECONOMICS | MITIGATION |
|---|---|---|
| Spreads +75 bps | ABS WAC increases ~60 bps; net benefit reduced 40% | Maintain warehouse as backup; flexible timing |
| Losses +50% | CE may increase 3-5%; proceeds decline | Robust performance monitoring; tighter credit |
| Market closed 6 mo | Warehouse carry cost of ~$1.5-3M | Adequate warehouse capacity; liquidity reserves |
| Rate shock +200 bps | Limited impact (floating rate assets/liabilities) | Natural hedge through floating-rate structure |

### PLAN FOR THE DOWNSIDE

The time to plan for adverse scenarios is before your first deal — not in the middle of a market disruption. Build contingency plans, maintain warehouse relationships, and ensure adequate liquidity to weather periods when ABS markets are unfavorable.

CHAPTER 8

# Optimizing Deal Economics

## Levers for Improving Economics

Once you understand the basic framework, there are several levers you can pull to improve the economics of each transaction.

### 1. Improve Collateral Quality

Higher-quality collateral (lower expected losses) directly reduces CE requirements and tightens spreads. Even modest improvements in underwriting — tightening credit criteria by 10-15 FICO points, for example — can measurably improve deal economics.

### 2. Optimize Deal Timing

ABS spreads are cyclical. Issuing during periods of strong investor demand and tight spreads can save 20-40 bps across the capital stack. Maintain flexibility to accelerate or delay issuance based on market conditions.

### 3. Grow Deal Size

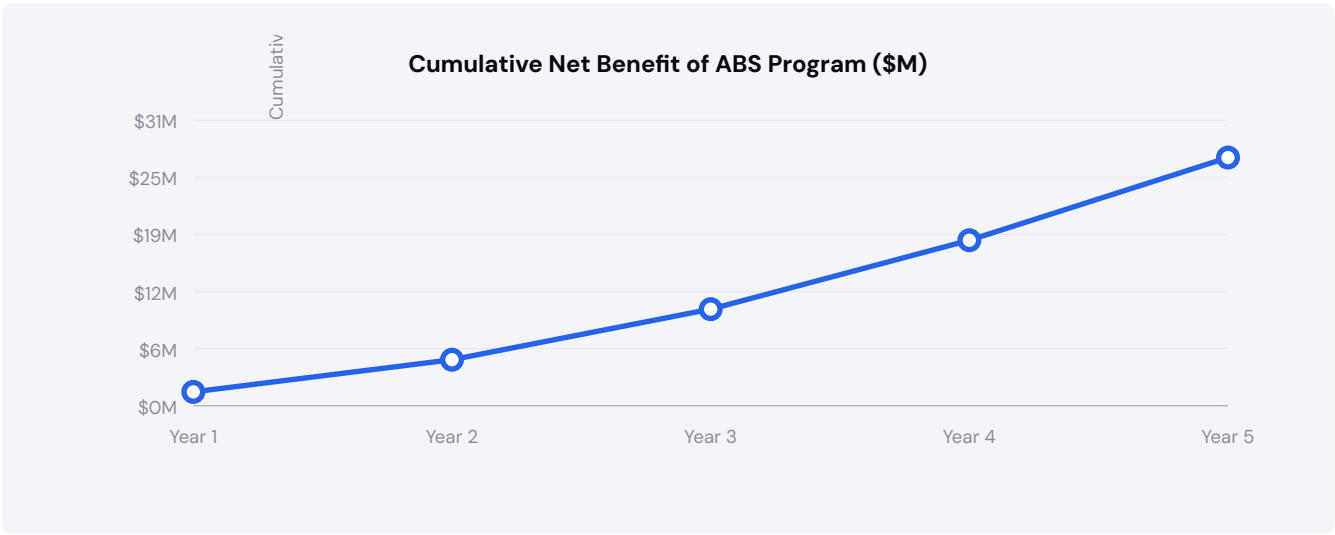
Larger deals spread fixed costs over a bigger base and attract more investor attention (larger deals are more liquid in secondary markets). Moving from $150M to $300M deals can reduce per-dollar issuance costs by 30-40%.

### 4. Build Investor Relationships

Repeat investors who are familiar with your collateral and trust your data provide more reliable demand and tighter pricing. Invest in investor relations between deals — quarterly updates, performance calls, and proactive communication.

### 5. Invest in Data Infrastructure

Better data leads to more precise rating agency models, which leads to lower CE requirements. Automated data pipelines reduce the operational cost and time of deal preparation. Both translate directly to improved economics.


Cumulativ
Cumulative Net Benefit of ABS Program ($M)
$31M
$25M
$19M
$12M
$6M
$0M
Year 1
Year 2
Year 3
Year 4
Year 5

CHAPTER 9

# Repeat Issuance Economics

## The Compounding Advantage

The true economic power of securitization emerges with repeat issuance. Each subsequent deal benefits from:

- Lower issuance costs: Legal templates, established rating agency relationships, and streamlined processes reduce per-deal costs by 40-50%.
- Tighter spreads: Investor familiarity with your collateral and demonstrated performance history tighten pricing by 30-60 bps over the first 3-4 deals.
- Higher advance rates: As performance data validates asset quality, CE requirements decrease and proceeds increase.
- Compressed timelines: Execution timelines shrink from 12-16 weeks (inaugural) to 4-8 weeks (repeat), reducing market timing risk.
- Operational efficiency: Automated data, reporting, and deal preparation reduce the internal cost of each transaction.

| METRIC | DEAL 1 | DEAL 3 | DEAL 6+ |
|---|---|---|---|
| Senior spread (bps) | 140-160 | 110-130 | 90-110 |
| Issuance cost (%) | 2.0-3.0% | 1.2-1.8% | 0.8-1.2% |
| Execution timeline | 12-16 weeks | 8-10 weeks | 4-6 weeks |
| CE requirement | 20-25% | 17-22% | 15-20% |
| Net proceeds (%) | 88-92% | 91-94% | 93-96% |

Illustrative progression for a consumer unsecured lending program.

## Building the Programmatic Platform

To capture the full benefit of repeat issuance, invest in infrastructure from day one: automated loan tape generation, standardized reporting, streamlined legal processes, and ongoing investor communication. The

marginal cost and effort of each subsequent deal should decrease meaningfully — and the economic benefit should compound.

# Appendix A: Glossary of Economic Terms

| TERM | DEFINITION |
|---|---|
| Advance Rate | Total rated bonds as a percentage of collateral balance; determines gross proceeds. |
| Blended WAC | Weighted average coupon across all rated tranches; your effective cost of ABS debt. |
| Credit Enhancement | Total structural protection for senior investors, expressed as a percentage of the deal. |
| Excess Spread | Difference between collateral yield and bond coupon + fees; first line of loss defense. |
| Gross Proceeds | Total par value of rated bonds sold to investors. |
| Net Proceeds | Gross proceeds minus issuance costs; actual cash received. |
| Overcollateralization | Excess of collateral balance over rated bond balance. |
| Residual | Cash flow remaining after all bond obligations are met; accrues to equity holder. |
| Subordination | Percentage of the capital structure that is junior to a given tranche. |
| WAL | Weighted Average Life — the average time until principal is returned to bondholders. |

# Appendix B: Model Assumptions Template

Use this template to organize the key assumptions for your securitization economic model.

| CATEGORY | ASSUMPTION | YOUR VALUE | SOURCE |
|---|---|---|---|
| Pool | Collateral balance | i | Loan tape |
| Pool | Weighted avg. coupon | i | Loan tape |
| Pool | Weighted avg. term | i | Loan tape |
| Pool | Weighted avg. FICO | i | Loan tape |
| Performance | Base-case annual loss rate | i | Static pool data |
| Performance | Recovery rate on defaults | i | Historical data |
| Performance | Prepayment speed (CPR) | i | Historical data |
| Performance | Delinquency rate (60+) | i | Current tape |
| Structure | Senior tranche size | i | Rating agency |
| Structure | Total CE requirement | i | Rating agency |
| Structure | Reserve account size | i | Structuring |
| Pricing | Senior spread estimate | i | Arranger guidance |
| Pricing | Mezz spread estimate | i | Arranger guidance |
| Costs | Underwriting fee | i | Arranger term sheet |
| Costs | Legal (total) | i | Counsel estimate |
| Costs | Rating agency fees | i | Agency proposal |
| Comparison | Current warehouse rate | i | Facility docs |
| Comparison | Current warehouse advance | i | Facility docs |

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