

Asset Securitization as a Means of Tourism Financing

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Abstract

Tourism is one of the world's largest industries and a particularly important issue is the financing of its development. Tourism and culture are significant elements of the region's economy and are likely to be major growth sectors. Tourism development in countries in transition ensures revenue growth, employment, development of the hospitality sector and infrastructure. The paper aims to draw attention to the possibility of applying asset securitization in the financing of tourism. State subsidies and bank loans do not provide sufficient funds and require new sources of funding. Securitization of assets enables the bond issue on the basis of specific, isolated assets such as loans. It also allows the bond issue and the collection of cash on the basis of the assets that will arise in the future. Tourism can achieve significant revenue today using securitization of future cash flows, where the collateral may be Vacation Ownership Receivables, tolls, credit card receivables, hotel revenues. There is a particularly important issue to provide funding by REITs and REMICs.

Keywords: *tourism industry finance, agro tourism securitization, future cash flow*

JEL Classification: *G21, G23, L83, Q14*

Introduction: the Importance of Tourism in the Modern Economy

The last decades of the 20th century and beginning of the 21st century have shown that tourism, as a world economy industry, according to all relevant indicators (transport tourists, foreign currency inflow etc) leads in relation to other sectors of the economy. The tourism sector is one of the fastest growing sectors of the global economy. Tourism is a sector which is closely associated with other sectors of the economy: traffic, agriculture, trade, spacious planning, energy industry and information technology. The development of tourism is followed by the development of the overall economy. At the same time, tourism recognizes the basic values of an area and keeps them (natural and cultural attractions of the certain destination, trip, accommodation, transport) in relation to the specific forms of tourism (cultural, rural, business, eco-tourism etc). Tourism development requires considerable financial resources. Besides hotels and other accommodation capacities, restaurants, shops and other facilities, the infrastructure is

also of high importance: road network, municipal infrastructure, gasification, development of the energy sector, ports, airports etc. Therefore, the active role of public and private sector is very important. International tourist developments represent only a small part of the overall tourism trends in the world. According to the relevant estimates, the domestic tourist turnover in many countries makes up 70% of the total tourism revenues. Taking on the role of leader and achieving a significant share of the global gross domestic product and total employment.

Tourism is among the top-job creating sectors because of its labour intensive nature and the significant multiplier effect on employment in other related sectors. The direct contribution of Travel & Tourism to the world economy grew by 3.1% in 2013, contributing US\$2.2 trillion to the world's gross domestic product (GDP) and 101 million jobs. The direct contribution of Travel & Tourism to GDP of EU in 2011 was USD 508.1bn (2.9% of GDP) and USD 506.8bn in 2012. The direct contribution of Travel & Tourism to GDP is expected to grow by 2.4% pa to USD 643.8bn (3.0% of GDP) by 2022. Travel & Tourism of EU generated 7,281,000 jobs directly in 2011 (3.3% of total employment). This (GDP and jobs) includes employment by hotels, travel agents, airlines and other passenger transportation services, restaurant and leisure industries directly supported by tourists (excluding commuter services). By 2022, Travel & Tourism will account for 8,299,000 jobs directly, an increase of 1.3% over the next ten years.¹ In 2013, the number of nights spent in tourist accommodation establishments in the EU28 reached a peak of 2.6 billion nights. The largest increases of the number of nights spent in tourist accommodation establishments in 2013 were recorded in Greece (+11.7%), Malta (+7.8%), Latvia (+7.3%), the United Kingdom (+6.5%), Bulgaria (+6.2%), Slovakia (+5.5%) and Hungary (+5.0%). In the EU28, the number of nights spent in tourist accommodation establishments by non-residents grew by 4.8% between 2012 and 2013, while nights spent by residents decreased by 0.8%. In 2013, the largest increases for non-residents were observed in the United Kingdom (+16.7%), Greece (+13.2%) and Latvia (+9.4%), and for residents in Greece (+6.7%), Estonia (+6.1%), Bulgaria and Slovakia (both +5.3%). These results are showing that tourism sector became an important activity for developing countries, regarding that countries from South East Europe have a significant increase in the number of nights. In order to demonstrate the importance of tourism sector in transition economies we will have collected the data of net occupancy rate of bed-places and bedrooms in hotels and similar accommodation in Serbia, Romania, Montenegro, Croatia, Bulgaria and Hungary (table 1).

Table 1: Net occupancy rates in bed places in the transition economies (2012) %

Country					
Serbia	Montenegro	Romania	Croatia	Hungary	Bulgaria
26.8	30.0	30.1	53.1	32.1	38.8

Source: <http://epp.eurostat.ec.europa.eu>

As it can be noticed, continental countries have less occupancy rate in bed places, which is important for further investments in accommodation and also other facilities for tourism development.

There is the growing presence of Central and Eastern Europe in the tourism sector. The government, in order to reduce unemployment, should enable and stimulate individuals to start their own business. The support of the government encourages entrepreneurship and the establishment of small and medium-sized enterprises in tourism. Tourism development requires not only the establishment of travel agencies and hotel capacities, but also restaurants, shops, shopping malls, parking lots, rural tourism etc. The last decades saw the emergence of new destinations and the transition from mass tourism into special interest tourism.

¹ http://www.wttc.org/site_media/uploads/downloads/european_union2012.pdf

Asset Securitization

Asset securitization allows the financing on the basis of assets used as collateral (pledge) for the securities issue. The collateral can include all kinds of loans (mortgage, student, agricultural, car loan), leasing (for cars, equipment etc), but also all other receivables that have predictable cash flow (tolls, airline tickets, hotel revenues and vacation ownership). The point of securitization is to have the receivables (credit, debt, assets) on the basis of which the bonds were issued that represent a guarantee for buyers of bonds that they will be paid on time (paid interest and principal on the maturity period). Securitization aims to transform non-liquid assets into liquid, i.e. loans and other receivables converted into securities. Funding is based on certain assets and its quality. The asset is taken from the balance sheet of the lender, so the credit risk is transferred to the other participants in the financial market. Securitized products carry the risk of the asset that is the collateral, but not the risk of the issuer as is the case with ordinary bonds. This feature allows financing the securitization of all the institutions that create assets. Securitization is done with the help of special purpose vehicles (SPV). The SPV buys loans or other assets of the originator, and on its bases it issues the securities. The originator, in most cases, has the role of the servicer: it collects interest and principal of the borrower, although it was sold. The raised money is forwarded to the SPV. As the obligations are paid on the basis of the asset that is collateral, financial funds are paid investors who bought the securities.

In the process of securitization, any loan or receivable can be used under the condition that it has a predictable cash flow. The process of securitization of assets has enabled the emergence of various types of securities. Depending on the collateral, we may distinguish mortgage-backed securities (MBS) and asset-backed securities (ABS). They are very popular with institutional investors, banks and other financial institutions. Securities arising from the process of securitization can be long-term and short-term, with the fixed and changeable interest rates, while the collateral may be depreciated and non-depreciated assets. Asset securitization has led to the creation of securities that are tailored as wished by investors. Structured securities allow redistribution of cash flow (pay-through) of the pool of assets in different tranches. Collateralized mortgage obligations (CMO) have mortgages as collateral, while Collateralized debt obligation (CDO) use non-mortgage loans and other assets. CMOs and CDOs are issued in more tranches of bonds. Senior tranches are purchased by institutional investors for their highest rank (AAA); tranche subordination is bought by sophisticated investors, while equity tranche is retained by the sponsor (arranger) of the transactions or is bought by hedge funds. Cash flow is distinguished by instalments (cash flow waterfall). The most senior class has the lowest coupon, while the equity tranche has no coupon. Equity tranche was ranked as the highest risk, but also the most profitable. If there is default in the pool, equity tranche bears the first loss (first-loss piece, FLP). When the senior tranche is paid, the payment of subordinated classes of bonds may begin.

Asset Securitization and Application in Tourism

Securitization in tourism may be used in case of:

- 1) Mortgage loans (financing through CMBS, REMIC, REIT),
- 2) Securitization of Vacation Ownership Receivables
- 3) Future flow securitization
- 4) Project finance.

Asset securitization allows for the raising of capital to finance the development of tourism. Regardless of the fact whether the capital investment is necessary for state or private sector, it is important to turn, in addition to banks, to the capital market. Bond issue on the basis of certain assets could bring a new source of funds. The collateral for the bond issue in the tourism

industry may include existing assets as well as assets that will arise in the future. From the existing receivables we use mortgage loans, loans for renovation and adaptation, loans for equipment, loans for small and medium-sized enterprises etc. It is necessary to provide refinancing, or entitle banks to sell the loans that they have approved. Banks approve loans for tourism development but the problem is that banks hold the granted loans until the maturity period in the portfolio. By selling the loans, the bank receives new funds and may approve new loans. The possibility of increasing funding would allow residents to get loans more easily at lower interest rates and to start business in tourism (rural tourism, restaurants, hotels etc.)

The application CMBS, REIT and REMIC in the financing of tourism

Commercial mortgage loans for the construction of accommodation facilities or loans to small and medium-sized enterprises in the tourism industry can be sold by the bank in the financial market. The customer transfers loans to the SPV to issue bonds. On the basis of the money raised from the collateral (commercial mortgage loans, loans for small and medium-sized enterprises) in the pool there will be payment of interest and principal to the investors in bonds. In other words, as borrowers pay monthly instalments, the SPV collects funds and financial payment obligations payable to the investors. Among the receivables that will arise in the future, there are hotel revenues (complete revenue that the hotel gains - room rent, restaurant, cafe, pool, gym, sauna and other services charged in the hotel), credit card receivables, tolls and so on. Entrepreneurs and small and medium-sized enterprises use bank loans and government subsidies. Likewise, in addition to cash grants, the government may impose tax exemption for certain activities (for example, in the period of the first few years), decrease tax rate for those who choose to deal with rural tourism etc. When loans are concerned, there are mainly commercial mortgage loans. If banks can sell commercial loans in the market, they will always be able to come up with liquid funds for finance tourism. Commercial mortgage loans are used to buy or build the commercial property that brings in revenue. This involves accommodation facilities, restaurants, shopping centres, sports and cultural events for tourists. If the collateral is the commercial real estate, the commercial mortgage-backed securities (CMBS) are issued. CMBSs are debt instruments secured by commercial property (hotels, offices, shops, factories, warehouses). CMBS may be issued according to the pool with one or more loans. Payments to investors in the CMBS depend on the cash flow that is collected from the commercial property. CMBS consists of multiple tranches with different risk and return.

Real estate investment trusts (REITs) are companies that invest in properties that generate revenue. REITs generate income from residential and commercial real estate. REITs invest in shopping malls, apartment buildings, office buildings, hotels, mortgage securities etc. In addition to investing in real estate and land, they purchase mortgage securities. Thus, these trusts would have a dual role in the development of tourism. First, there will be investment in real estate that is related to tourism. Second, there is investment into securities; in other words, they finance those that issue mortgage securities. REITs issue shares and collect the capital, but they can also issue debt instruments (bonds, CMBS). REITs are pass-through entities and (in the U.S.) do not have to pay federal income tax at the corporate level. REIT must (1) pay dividends to shareholders equalling at least 90% of its taxable income and (2) more than 75% of total investment assets must be in real estate assets.² A REIT can invest in different types of real estate assets. Equity REITs are owners of real estate properties (retail, commercial, residential real estate). Mortgage REITs do not usually own real estate properties. Mortgage REITs can lend money directly or indirectly: Mortgage REITs can invest in mortgages and mortgage-backed securities, and Mortgage REITs can originate mortgage loans and securitizing mortgages and mortgage-backed securities. A hybrid REIT function as both equity REITs and mortgage

² Fabozzi J. Frank, *The Handbook of Financial Instruments*, John Wiley & Sons, Inc., 2002., pg. 397

REITs. Lodging REITs invest in hotels and resorts. Industrial REITs invest in industrial properties, warehouse etc. Residential REITs invest in apartments, houses etc.

Real Estate Mortgage Investment Conduit (REMIC) is a pass-through vehicle created for commercial mortgage loan securitization. REMICs invest in mortgages (single family, multifamily mortgages) commercial mortgages and federal agency pass-through securities. REMICs are typically exempt from tax at the trust level. Since 2003, roughly \$110 billion of lodging mortgage debt has been originated and securitized into REMICs in the United States, collateralized by slightly over 18,000 lodging properties. The importance REMIC is seen in financing as there are about 51,000 hotels in the USA.³ Hotel mortgage loans are transferred into a REMIC and REMIC issues collateralized mortgage obligations (CMOs). In order to facilitate the issue of CMO, the Congress has allowed the establishment of REMIC (Reform Act of 1986). Today, almost all CMOs are issued over REMIC because of tax relief. CMOs were created in order to protect investors from the risk of early repayment of the mortgage loan. The risk of early repayment is redirect to different tranches, whereby investors can choose instalment that suits them in terms of risk and return. CMO does not eliminate the risk of early repayment, just relocates the holder of tranche that is willing to take this risk. There are different types of collateralized mortgage obligations (CMO): sequential-pay CMOs, Z bond (accrual tranches), planned amortization class bond (PAC), mortgage strips. Sequential Pay CMO means that there is the order in the disbursement according to seniority. The first in the payment of the principal is more senior tranche (A) and when the holders of these tranches are paid the entire principal, the payment of the next class may begin. Classes B, C and D receive interest but no principal. After payment of the investors who bought the Tranche A, there is payment of the principal of Tranche B. The process continues until all issued tranches are paid. Z-bonds (Z-Tranche) are usually subordinate classes with the issue of Sequential Pay CMO. Z-bonds do not get either interest or principal until all prior classes are paid (zero-coupon bond). Z-Tranche is usually not ranked, and if it is ranked, it is below investment grade (speculative grade). Each tranche is the protection of a higher tranche, while the Z-Tranche is a credit enhancement to all previous classes. REMIC uses Z-Tranche, which has the "first loss" position, which means that investors who buy them first are to bear the loss. In practice, there are different forms of the resulting Z-Tranche. Trick Zs allow the accumulation of interest on or off under certain conditions (e.g. a certain date). Jump Zs are bonds that provide priority in the payment of principal when the early repayment increases. Jump Zs "jumps" ahead of other classes in order to receive priority in the payment of the principal.⁴

Securitization of Vacation Ownership Receivables

Vacation Ownership (Fractional Ownership, Timeshare) provides rights to use the property for specific time periods. Buyers usually make payments in monthly instalments over a specified period of time and annual maintenance fee. In return, they get an apartment that can be used for certain numbers of years. The developer then sells time-based intervals to buyers, and he can use specific unit for a specific time period. Asset securitization is an important means of financing hotels which operate on the principle of timeshare. Asset securitization enables the timeshare developers to re-use the original seed capital repeatedly in order to expand their developments. The developers can expand rapidly without waiting for their first resort's entire timeshare payments to be realized over a number of years. Timeshare buyers usually make payments in monthly instalments over a specified period of time. But the developer does not need to have their entire capital tied up until the timeshare buyer clears all their payments. The process of securitization enables the resort developer to sell off the accounts receivables of

³ <http://www.hvs.com/article/5017/the-alarming-tidal-wave-of-hotel-mortgage-loan>

⁴ Lowell Linda in *The Handbook of Mortgage-Backed Securities*, Sixth Edition, McGraw-Hill, 2006. pg. 505. (Editor Fabozzi J. Frank)

various timeshare buyers, and re-deploy the capital into the expansion of the business.⁵ Hilton, Marriott, Melia, Hyatt, Four Seasons, Disney, Accord Hotels have used Vacation ownership securitization.

The financing of Vacation Ownership is usually provided by developers. Vacation Ownership loans have the maturity of 3 to 15 years. Also, the purchase (or refinancing) may be made through bank loans and real estate brokers who deal with timeshare. There is also credit card renting. Timeshare owners who have taken a loan from the developers can refinance it with bank loans, home equity loans, or transfer the remaining balance to a credit card. The collateral for the securitization are the vacation ownership loans on whose basis vacation ownership loan backed notes are issued. Developers often pool and securitize balances due from customers. The SPV holds the assets (loans and funds) in trusts, and sells asset backed securities (ABS). Some of the popular types of asset backed securities are formed out of house mortgages (MBS), commercial loans (CMBS) and home equity loans. Mortgage backed securities (MBS) are used for vacation ownership financing. Home Equity Loans are loans based on the equity in the borrower's home as collateral. HEL loans can also be used for timeshare financing. Timeshare companies issue collateralized debt securities (CDO). Securitization of Vacation Ownership Receivables is used by large developers that need large-scale funding. Costs are high and above all underwriting fees, credit enhancement (insurance, bank guarantee), credit rating agency costs, legal advice, accounting fees etc. Nevertheless, the government might help to solve this problem. The existence of state agencies that buy up receivables of tourism and issue bonds, or at least give guarantees for the bonds, would largely facilitate financing.

Diamond Resorts International Inc. is financed by the method of securitization. Diamond Resorts Owner Trust 2013-2 issued the bonds in the amount of \$225 million out of which \$213.15 million are AA rated vacation ownership loan backed notes and \$11.85 million of A+ rated vacation ownership loan backed notes. The notes have interest rates of 2.27% and 2.62% respectively, for an overall weighted average interest rate of 2.29%.⁶ In August 2013, Marriott Vacations Worldwide Corporation carried out securitization of the pool with \$263 million of vacation ownership loans which was purchased by MVW Owner Trust 2013-1 and issued the bonds in the amount of \$250 million. Two classes of Notes were issued by the Trust: \$224 million of Class A Notes and \$26 million of Class B Notes. Wyndham Worldwide Corporation, through Sierra Timeshare 2014-1 Receivables Funding LLC, issued \$425 million of asset-backed notes. Out of that, there were \$328 million of A rated notes and \$97 million of BBB rated notes. The notes were backed by vacation ownership loans.

Future flow securitization

Securitization allows for the receivables arising in the future to be used as a source of financing. Investors who buy securitized securities are interested in the cash flow that brings assets, regardless of whether there are assets in the balance sheet or they will arise in the future. Future flow securitization means that the originator (bank, company) sells its receivables that will arise in the future to the SPV. The SPV issues securities. Future flow securitization is very popular in countries in transition. The collateral includes export receivables from the sale of oil, gas, coffee, agricultural products, and future receivables by credit card (Visa, MC), diversified payment rights (DPRS) etc. Future flow securitization has allowed many investment grade borrowers in developing countries to pierce the sovereign credit ceiling and obtain financing at

⁵ www.vacationtimesharerentals.com

⁶ www.DiamondResorts.com

significantly lower interest rates and for longer duration.⁷ In tourism, the future revenues include hotel revenues, tolls, receivables from credit cards etc.

Hotel revenues

Hotels revenue is used as collateral for the bond issue. In the United States it is very popular to tax-exempt financing for hotel projects. Under U.S. federal tax law, bonds for a hotel project can only be tax-exempt if the property is owned by a state and local governmental entities. This benefit is especially used by convention headquarters hotels and airport. Convention centres attract a large number of visitors and this has a positive impact on the local economy. Congress tourism enables full accommodation capacities, but also going to shops, restaurants, car rental and others. Therefore, it is crucial that the hotels are near the convention centre. The hotels in which the participants of a convention stay are called "headquarters hotels". The use of tax-exempt financing for hotel projects means that the state or local self-government (municipality, province, city) enters into partnerships with private companies to build the hotel. Private companies involved in the business are developers and hotel operators (known hotel chains of Sheraton Operating Corporation, Hilton Hotels Corporation, Hyatt Corporation etc). The owner of the hotel that will be built is the state or city, through the company that is established specially for this purpose. The city or municipality cannot build a hotel and cannot operate it, so they use the services of private companies.

In order to build a hotel, the city may establish a public-sector entity that is a single-purpose entity created to develop, finance and own the hotel. The assets owned by the single-purpose entity are hotel revenues and the liabilities are bonds that they have issued. In this way, assets and liabilities of the city are separated and cannot be used for payment of receivables by investors. In other words, the investors may seek payment only from hotel revenues. Bonds are issued in tranche, and senior/junior subordination is used. Lower tranches often have additional security because they are riskier. The last tranche is usually bought by the private-sector project participants (developer, hotel operator). The city owns the hotel, but the construction is made by a privately-owned company (developer) who selects contractors and supervises works. After the construction of the hotel, the city remains the owner and the hotel chain assumes operation of the hotel under its name. Since it is not the owner of the hotel it gains profit on the basis of asset management fees.

In April 1999, the Sacramento City Financing Authority issued senior bonds (\$92.8 million) and subordinate bonds (\$4.1 million) to finance the construction of a 500-room convention centre hotel to be operated by Sheraton Operating Corporation under a Sheraton flag. The Hotel Owner is the Sacramento Hotel Corporation, a non-profit corporation established as an instrumentality of the City of Sacramento. Bonds were secured by the net revenues of the hotel and by the net revenues of City-owned parking garage located across the street from the hotel.⁸

In June 2001, City of Austin, Texas created a non-profit public facilities corporation Austin Convention Enterprises, Inc to finance and build hotel and garage. The Austin Convention Enterprises Inc. issued bonds in a total principal amount of \$265 million to finance the construction of an 800-room and a 600-space underground garage. The Hotel Owner is the Austin Convention Enterprises Inc and the hotel will be operated by Hilton Hotels Corporation under the Hilton flag. The first tier bonds (\$109.665 million) were rated Baa3 (Moody's) and BBB- (Standard & Poor's). The second tier bonds (\$134.95 million) were insured by ZC Special Insurance Co., and bonds carried a higher rating than the first tier bonds and were

⁷ Ketkar Suhas, Ratha Dilip: Recent Advances in Future-Flow Securitization, *The Financier* VOL. 11/12, 2004-2005., pg. 3.

⁸ Magan Jenna, Davis Roger, Israel Perry Liever Michael Hotel Projects: Financing With Tax-Exempt Bonds, Orrick, Herrington & Sutcliffe LLP 2001-2002, pg. 45

therefore sold to the public. The third tier bonds (\$20.5 million) were purchased by the developer and the hotel operator.⁹

Credit card merchant voucher receivables

Credit card merchant voucher receivables securitization enables fundraising on the basis of the sale of future receivables from the use of payment cards (credit, debit). This is particularly important for countries in transition and developing countries, which are visited by many tourists, business people, because they use the cards when paying local merchants (stores, restaurants, hotels, ATM etc). Credit card merchant voucher receivables can be a significant source of income for banks. The countries visited by many tourists can benefit from tourism-related expenditures, because banks can sell future credit card receivables. Tourists pay a lot of products and services when they are abroad. Merchants make credit card voucher to the local bank, and the bank pays cash for vouchers (less a transaction fee). The bank then obtains dollars from the credit card company. Banks in transition countries can sell future credit card receivables and thus obtain the funds. The bank gets the money that can be used for lending. The bank sells future credit card receivables voucher to offshore SPV. The SPV issues bonds and sells to investors. Investors will receive interest and principal on the maturity date of the bond, based on spending and credit card payments in a country in transition. After the sale, credit card companies (Visa, MasterCard, American Express) send the cash to the offshore SPV instead to a local bank. Credit and debit cards voucher receivables securitization is used in the Republic of South Africa, Peru, Mexico, Egypt, Turkey etc.

In 2000, Rand Merchant Bank (RMB) from South Africa carried out US\$ 250 million worth of Visa, MasterCard and Cirrus voucher receivables. Banco de Credito del Peru sold the future receivables to offshore SVP - BCOL Master Trust. Bank instructed Visa to transfer all future payments on credit card vouchers to offshore SVP - BCOL Master Trust. Jamaican Credit Card Merchant Voucher Receivables Master Trust's issued \$125 million worth bonds in 2001, with the maturity date until 2006. The securitized receivables consist of all of Commercial Bank Jamaica Ltd.'s (NCB) existing and future rights to receive U.S. dollar -denominated payments from Visa International and MasterCard International Inc. These receivables come from NCB's acquisition of electronic or paper transaction vouchers generated by the use, in Jamaica, NCB sold the receivables created, and to be created under the credit and debit card programs, to NCB Merchant Voucher Receivables Ltd. (NCB MVR), a Cayman Island special purpose company. MasterCard and VISA agreed to make all future payments to an offshore SPV. The payments for which cards are used include as follows: travel and tour agents, hotels resorts, airline, car rental, restaurants, cafes, shops, amusement parks, health services, gas stations, flights and others. Travel agencies make up a large percentage of merchant charges, but there are also airlines (Air Jamaica makes up 16% of the total merchant charges).¹⁰

Project finance

The project provides funding for financing the projects of great value. It is often used for financing large infrastructure projects such as oil and gas exploration, refineries, pipelines, electric power generating facilities, telecommunications, toll roads, hospitals and schools. Project financing is particularly important for countries in transition. The reason is that these countries have not developed financial market and cannot collect the capital for major projects from local investors. Project financing attracts capital from investors from all over the world. The development of tourism depends on the capital investment in the countries in transition and developing countries. The capital is needed if the country wants to build infrastructure – road

⁹ Magan Jenna, Davis Roger, Israel Perry Liever Michael Hotel Projects: Financing With Tax-Exempt Bonds, Orrick, Herrington & Sutcliffe LLP 2001-2002, pg. 47

¹⁰ Kochubka Gary, Flores J. Juan, Olivares David, New Issue: Jamaican Credit Card Merchant Voucher Receivables Master Trust, Standard & Poor, 2001, pg 8.

network, tunnels, bridges, energy, water supply and sewerage network, to make gasification and others. States may use project finance to build the necessary infrastructure for tourism development. If the state cannot participate as a sponsor, this work can be handed over to private companies. The capital is collected from sponsors, commercial and investment banks, multilateral and development finance institutions, export credit agencies, insurance companies, investment funds, pension funds, hedge funds etc. A project financing is based on equity financing and debt financing (loans, bonds) through the project company. The project company is established by the sponsor in order to raise capital for the funding of the project. Project sponsors (companies, countries) form a joint company for the construction and funding of a particular project. Project finance is based on future-flow securitizations and issue of Project finance CDOs. The project company is a separate legal entity - Special Purpose Vehicle (SPV). The purpose of establishing the SPV is to raise capital for the project. The SPV collects the capital from sponsors (founder), from the issue of shares and bonds and from taking bank loans. Project finance CDOs are sold through public or private debt placements. The investors are pension and investment funds, hedge funds and investment banks. Project finance CDOs are CDOs backed by loans project (Project Finance Close) Bonds Project Finance CBOS), or lease collateral.

Agro-Tourism

Development opportunity for countries in transition is reflected in the creation of new tourism products and adapting to offer special interest tourism. Agro tourism can have a special place in the creation of this supply and by investing in their development there will be positive economic effects. Agro tourism means that tourists know each other and participate in activities in rural areas (agriculture, events, gastronomy, folklore, ethnology, crafts and other activities on the farm). The strong influence of the tourism sector, especially with the active involvement of the government, could be used as an ideal solution for diminishing the economic power of the village. Agro tourism can be a factor in the development of neglected rural areas. Agro tourism is getting more support in developed and countries in transition. Tourists get the opportunity to learn about the activities of farmers. Attracting tourists not only brings revenue to farms, but also allows the development of the region. The farmer gets additional income from visiting tourists. Agro tourists can help with jobs on the farm, in the field or orchard, and they may also ride horses, drive a tractor, milk cows etc. Agro tourism can be financed through loans, especially mortgage, then loans for working capital, lease for the purchase of machinery, loans for the purchase of livestock, plants and others. The government may give subsidies, tax-exempt or reduce the tax rate for entrepreneurs who want to deal with agro tourism. Likewise, it is necessary to stimulate not only the population living in the countryside to begin agro tourism but also to attract people who have houses in the countryside and live in the city. Stimulation and support of the state may prevent the abandonment of rural areas and unemployment. Funding allows people to stay in rural areas, but also to start their own business. In addition to loans to purchase home, they can also use loans for renovation and the like. There is need for loans for purchase of seeds, land, livestock, machinery or the construction of buildings. Agro tourism development will affect the development of the village and the entire region, and there will be necessary investments of municipalities and villages. This will include the construction of road networks, water supply and sewerage network, gas, bus lines, renovation of buildings or building new ones, establishing the cinemas, shops, sports fields and halls and the like. Loans and subsidies will be necessary to municipalities and villages where the population is engaged in agro tourism.

Asset securitization has already been used for financing agriculture in many countries in transition, especially in Latin America. Agricultural loans are used as collateral for securities issuance. Agricultural loans securitization is applied in Brazil (Brazil Agrosec Securitizadora

Company). Securitization based on other collateral means the use of repurchase agreement and warehouse receipt for the bond issue. The former is used in Mexico and the latter in Colombia. The financing of agriculture also involves the application of future flow securitization. An example is a Peruvian company Drokasa. The collateral for the issuance are future receivables from buyers of agricultural products. Therefore, as loans and other assets for funding of agricultural development are securitized, in the same way the loans for the development of agro tourism can be used as the collateral.

The Role of the Government in the Development of Securitization in Tourism

Asset securitization can be conducted by the state and private sector. In order to speed the development of tourism and implementation of securitization for funding, the role of the state is preferred. A very important question is who will purchase receivables and carry out securitization. In addition to the sale of receivables, the originators can be carried out securitization through the trusts they established themselves. The existence of the buyer of receivables enables the continuity in financing. The buyer of receivables and the issuer can be either private or state-owned SPV. The existence of state agencies would significantly facilitate the financing, as is the case on the market of residential mortgage loans. State agencies can perform two functions. The first is to buy the loans granted by banks to finance tourism. In this way, the bank would receive fresh capital that could be used to grant new loans. Also, the sale of loans means that they are taken out of the bank balance sheet so the credit risk and interest rate risk are eliminated. The agency would be funded by the issue of bonds that investors would buy on the financial market. The first level of protection for investors includes loans that the agency has bought. The second level of protection is subordination of issued bonds, i.e. the existence of instalments, insurance, bank guarantees and other forms of credit enhancement. Another important role of the agency may be providing guarantees to banks. By giving a guarantee the agency assumes the risk to itself; in other words, if the borrower fails to fulfil obligations to the bank, the agency will do it. The guarantee of the agency may not be 100%, but if they guaranteed for 50% of loans, banks would be encouraged to lend to a greater extent to the development of tourism. The agency can issue collateralized debt obligation (CDO), but it keeps the equity tranche. Therefore, the agency is ready to be the first to bear the loss if the transaction is not successful. In this way, investors are encouraged to buy securitized securities. The third role of the state agency is to provide guarantees for securitized bonds of the private sector. This means that the private sector through the SPV buys loans from banks, issues CMO or CDO, and the state agency provides a guarantee that the obligations to the investors will be fulfilled. State guarantees may be explicit or implicit. The existence of the state agency or the agency of the mixed ownership would be particularly important for the countries where tourism is the most important industry. If it is not possible to establish a special agency that would perform securitization, the state can provide guarantees through its ministry of tourism. This would be similar to government agencies operating in the residential mortgage market.

An example is Tourism Finance Corporation of India Ltd (TFCI) specialized in the financial tourism industry. The shareholders are IFCI Ltd, SBI Bank of India, United India Insurance Co. Ltd, LIC The Oriental Insurance Co. Ltd, Mutual Fund her Banks/ Financial Institutions Foreign Institutional Investor. TFCI provides financial assistance to enterprises, for development of tourism related activities like hotels, restaurants, holiday resorts, amusement parks and complexes for entertainment, education and sports facilities, safari parks, convention halls, all forms of transport industry, air-taxis, travel and tour operating agencies, tourism emporia, sports facilities etc. The forms of Financial Assistance which are provided by Tourism Finance Corporation of India Ltd (TFCI) are rupee loan, underwriting of public issues of shares/debentures, guarantee of deferred payments and credit raised abroad, equipment finance,

equipment leasing assistance under suppliers' credit working-capital financing takeover financing advances against credit-card receivables, Loan / Equity syndication services. TFCI provides research and consultancy services to the tourism industry in general and to the investors in tourism industry in particular.¹¹

Conclusion

Tourism brings the inflow of foreign exchange into the country, increases employment, leads to an increase in domestic and foreign investments and increased activity of the state to build infrastructure. The financing of tourism, especially in countries in transition, is based on bank loans and state grants. The application of securitization can bring significant resources to countries and companies that want to invest in tourism. Securitization aims to transform non-liquid assets into liquid, i.e., loans and other receivables are converted into securities. Securitization is done with the help of special purpose vehicle (SPV) that buys loans or other assets from the originator and issues securities. Besides mortgage-backed securities (MBS) and asset-backed securities (ABS), there is the application of structured securities that allow the redistribution of cash flow from the pool of assets in different tranches (CMOs and CDOs). Securitization in tourism can also be used with mortgage loans (financing through CMBS, REMIC, REIT), securitization of vacation ownership receivables, assets that will arise in the future and project finance. The bank can sell commercial mortgage loans for the construction of accommodation facilities and loans to small and medium-sized enterprises in tourism on the financial market. The buyer transfers loans to the SPV, which issues CMBS and CMOs. Real Estate Mortgage Investment Conduit (REMIC) invests in mortgages (single family, multifamily mortgages) commercial mortgages and federal agency pass-through securities. Real estate investment trusts (REITs) are companies that invest in the real estate that brings profit. REITs generate income from residential and commercial real estate. REITs invest in shopping malls, apartment buildings, office buildings, hotels, mortgage securities etc. Hilton, Marriott, Melia, Hyatt, Four Seasons, Disney, Accord Hotels have used Vacation ownership securitization. The collateral for securitization are vacation ownership loans and on the basis of them vacation ownership loan backed notes are issued. Developers often pool and securitize balances due from customers. The SPV holds the assets (loans and funds) in trusts, and sells asset backed securities (ABS). Some of the popular types of asset backed securities are formed out of house mortgages (MBS), commercial loans (CMBS) and home equity loans. Mortgage backed securities (MBS) are used for vacation ownership financing. Future flow securitization is done on the basis of hotel revenues, credit card merchant voucher receivables, credit card receivables, toll, sports and events. All these instruments allow for the capital to be collected which the state and the private sector can invest in order to develop tourism in the country. Hotels, restaurants, shopping malls, shops or parking garages are financed by loans and subsidies. Agro tourism is also funded in these ways. This includes the purchase and renovation of houses, purchase of livestock, plants, machinery, investment in rural municipalities, road construction etc. It requires a lot of money. Sales of loans and other assets allow the lender to come up with the funds to get new loans, but also to transfer interest rate risk and defaults on financial markets. The existence of government guarantees for approving loans in certain sectors or for bonds issued on the basis of the certain assets (e.g. loans for agro tourism) encourages banks to approve these loans, and the increasing number of approved loans reduces interest rate and loans are cheaper and more accessible for those who want to invest in tourism.

¹¹ <http://www.tfcilt.com/>

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