

SFA Research Corner

How Capital Rules Shape Securitization

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Banks originate credit, capital market teams structure and distribute it, and a broad range of investors—asset managers, pension funds, hedge funds, and insurance companies—ultimately fund it. For banks that make loans and insurance companies that invest in bonds backed by these loans, the decision is not just based on credit risk alone but are governed by capital rules, which determine how much capital they must hold against different assets. While capital rules are institution-specific, their effects extend beyond them—shaping not only which assets gets held or sold, but also which assets are originated and where liquidity develops across markets.

The Banks and the Basel III Endgame

When a bank makes a loan, it faces a choice: hold the loan on its balance sheet (or some portion of it) or package it into a securitization and sell it to investors. That decision is often largely influenced by how much capital that bank is required to maintain to support the loan. Holding a loan on balance sheet ties up capital that must be reserved against potential losses, limiting how much additional lending a bank can undertake. By contrast, securitizing the loan can free up that capital, and put it back to work via new lending. The more capital-efficient that process is, the more compelling securitization is as a funding tool.

When securitization provides meaningful capital relief, banks are more likely to originate and distribute loans—freeing up balance sheet capacity that allows them to continue lending, which keeps credit moving more efficiently through the system. That flow is then picked up by the capital markets, as newly originated loans are pooled and packaged into asset-backed or mortgage-backed securities that are purchased by investors who provide the funding that allows credit to scale beyond bank balance sheets.

But when securitization does not receive favorable capital treatment and banks must hold just as much (or more) capital even after selling the loans, the incentive to securitize weakens. In that scenario, banks are more likely to keep loans on their balance sheets, use up their capital more quickly, and slow new lending. Over time, markets will likely thin out, and credit will become more expensive and harder to access.

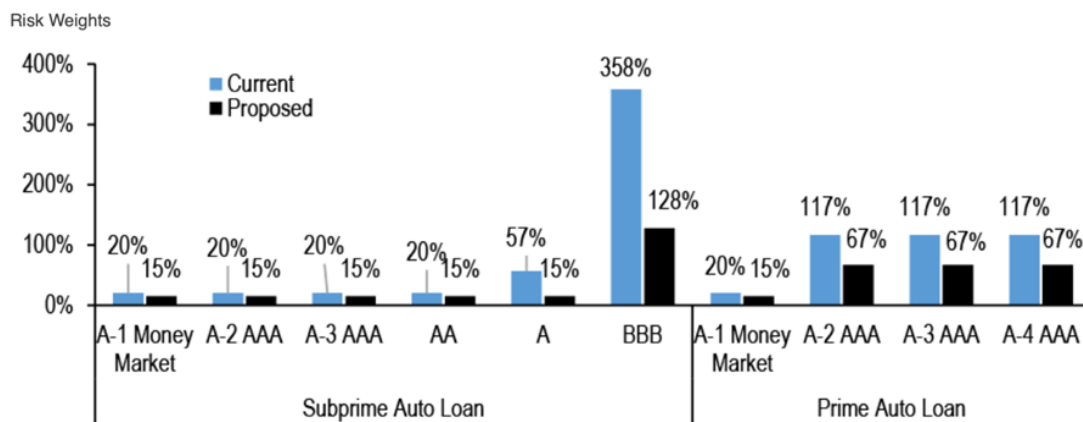
This dynamic has been at the center of the Basel III Endgame discussions, which began in earnest in the U.S. in 2023 following a set of bank capital rule proposals issued by the Federal Reserve. These proposals would have made securitization more capital-intensive, particularly through an increase in the “p-factor,”¹ a multiplier that increases the capital required for securitized exposures. It reflects a view that securitizations can introduce additional risks—such as structural complexity or model uncertainty—that may not be fully captured elsewhere. The higher the p-factor, the larger the required capital buffer, and the more expensive securitization becomes relative to holding loans directly.

¹ The p-factor directly influences the economics of securitization and, in turn, banks’ willingness to use it as a funding and risk transfer tool. In practice, it acts as a multiplier that makes securitization more capital-intensive than holding the underlying assets directly. This concept is known as “securitization capital non-neutrality.” The higher the p-factor, the more extra capital banks have to hold for securitized assets compared to holding the loans directly, effectively reducing the capital efficiency of securitization and discouraging its use as a credit risk transfer tool.

The Federal Reserve’s March 2026 [revised](#) proposal suggests regulators are weighing these considerations carefully. At a high level, the proposal, which is currently in a 90-day comment period, aims to “better align minimum requirements with risk,” while preserving the overall strength of the framework. Notably, the Fed’s proposal also does not increase the p-factor, avoiding what many market participants—including the Structured Finance Association ([SFA](#))—had warned would be a significant rise in capital requirements for securitization, with potential impacts on credit availability and market liquidity.

The proposal also introduces a look-through approach, allowing a banking organization to assign a senior securitization exposure a risk weight equal to the weighted average risk weight of the underlying exposures when sufficient data is available, improving risk sensitivity. In addition, the proposed reduction in the risk-weight floor from 20% to 15% further signals a recalibration toward better alignment with underlying risk. According to recent analysis by [J.P. Morgan](#), this change is expected to lower capital charges across CMBS, RMBS, and ABS with senior and highly rated tranches likely benefiting most, and more junior tranches seeing improvement or, at a minimum, no change relative to current levels.

How Lower Risk Weights Reduce Capital Requirements for Auto ABS (an Illustrative Example)



Source: J.P. Morgan

Taken together, these proposed revisions have been viewed by SFA as a positive step toward a more balanced and risk-sensitive capital framework—one that supports the continued flow of credit to households and businesses, even as the broader proposal remains subject to further analysis during the comment period.

Insurance and the NAIC

On the investor side, capital rules play a similar role. When capital treatment is well aligned with securitized risk, insurers are more willing to allocate investment capital to securitized assets—supporting consistent demand and helping sustain that flow of credit through the market. When it is not, demand can shift, and that flow can slow or become more uneven.

That dynamic is at the center of the current conversation between the National Association of Insurance Companies (NAIC) and insurers.

With bond holdings approaching \$5.5 trillion, as of year-end 2024, of which roughly \$1.4 trillion can be attributed to securitized products, insurance companies have become increasingly important buyers of securitized assets—particularly in higher-yielding segments of the market. In 2025, total bond acquisitions increased by roughly \$1.5 trillion, with \$486 billion allocated to securitized products, according to [J.P. Morgan’ Securitized Products Insurance Quarterly Update](#), underscoring the sector’s growing role in insurer portfolios.

In the U.S., insurers operate under Risk-Based Capital (RBC) requirements, which determine how much capital they must hold against their investments. Historically, RBC has evolved through targeted, often reactive updates. The NAIC’s current effort—supported by [Bridgeway Analytics](#)—is shifting toward a more structured governance framework, anchored in Principles adopted in December 2025.

Bond Breakdown by Insurer Type, Year-End 2024 (BACV* \$ in Millions)

| Bond Type | Life | P/C | Health | Title | Total | % of Total |
|-------------------------------------|------------------|------------------|----------------|--------------|------------------|-------------|
| Corporate Bonds | 2,325,400 | 567,628 | 83,414 | 3,210 | 2,979,652 | 54.9% |
| ABS and Other Structured Securities | 555,332 | 125,157 | 18,702 | 78 | 699,268 | 12.9% |
| Municipal Bonds | 192,555 | 222,558 | 18,405 | 806 | 434,323 | 8.0% |
| U.S. Government | 148,188 | 186,780 | 30,522 | 618 | 366,108 | 6.7% |
| Agency-Backed RMBS | 124,489 | 149,700 | 31,585 | 772 | 306,547 | 5.7% |
| Private-Label CMBS | 153,590 | 45,032 | 9,387 | 11 | 208,020 | 3.8% |
| Private-Label RMBS | 105,788 | 35,257 | 3,900 | 3 | 144,948 | 2.7% |
| Bank Loans | 103,820 | 16,508 | 2,212 | 213 | 122,753 | 2.3% |
| Agency-Backed CMBS | 40,659 | 36,168 | 2,386 | 75 | 79,288 | 1.5% |
| Foreign Government | 47,342 | 20,996 | 1,141 | 354 | 69,833 | 1.3% |
| Exchange-Traded Funds (ETFs) | 5,854 | 5,727 | 1,485 | 13 | 13,079 | 0.2% |
| Other | 94 | 307 | 120 | 10 | 531 | 0.0% |
| Total | 3,803,110 | 1,411,817 | 203,260 | 6,163 | 5,424,350 | 100% |
| % of Total | 70.1% | 26.0% | 3.7% | 0.1% | 100% | |

*BACV=Book Adjusted Carrying Value

Source: [NAIC Capital Markets Special Report, May 2025](#)

At the March 2026 annual meeting, NAIC advanced that effort by reviewing the new Principles, gathering industry feedback on gaps and inconsistencies across the framework, and introducing a more formal decision process—through a flowchart—to guide how new risks should be incorporated. At a high level, the framework is focused on a few core questions: Are important risks being missed? Are similar risks treated differently across the Life, P&C, and Health insurance sectors in ways that lead to inconsistent outcomes? And is there sufficient data to measure those risks appropriately?

Insurance industry feedback, as presented at the annual meeting, broadly supports a more structured and consistent approach, while cautioning against unnecessary complexity. Amnon Levy, founder of Bridgeway Analytics, pointed out “a range of differences and gaps across life, property & casualty, and health formulas regarding the treatment of investments, which is the primary overlapping component across the three.” Levy cited the American Academy of Actuaries letter, which explains that “attempting to comprehensively cover all material risks needs to be balanced with complexity” and that “creating an overly complex approach may increase model risk if there is inadequate model governance.”

In sum, bank and insurance regulatory capital rules determine not just how much securitized debt is created, but also how efficiently it flows through the financial system. As both frameworks evolve, the key question is not simply how much capital institutions must hold but how those rules shape the markets themselves. Over time these changes can have enduring impact, influencing which assets are originated, how they are financed and where liquidity ultimately concentrates.