

Exploring the rise of originate-to-distribute (OTD) models

Opportunities and challenges for banks in the secondary loan trading market



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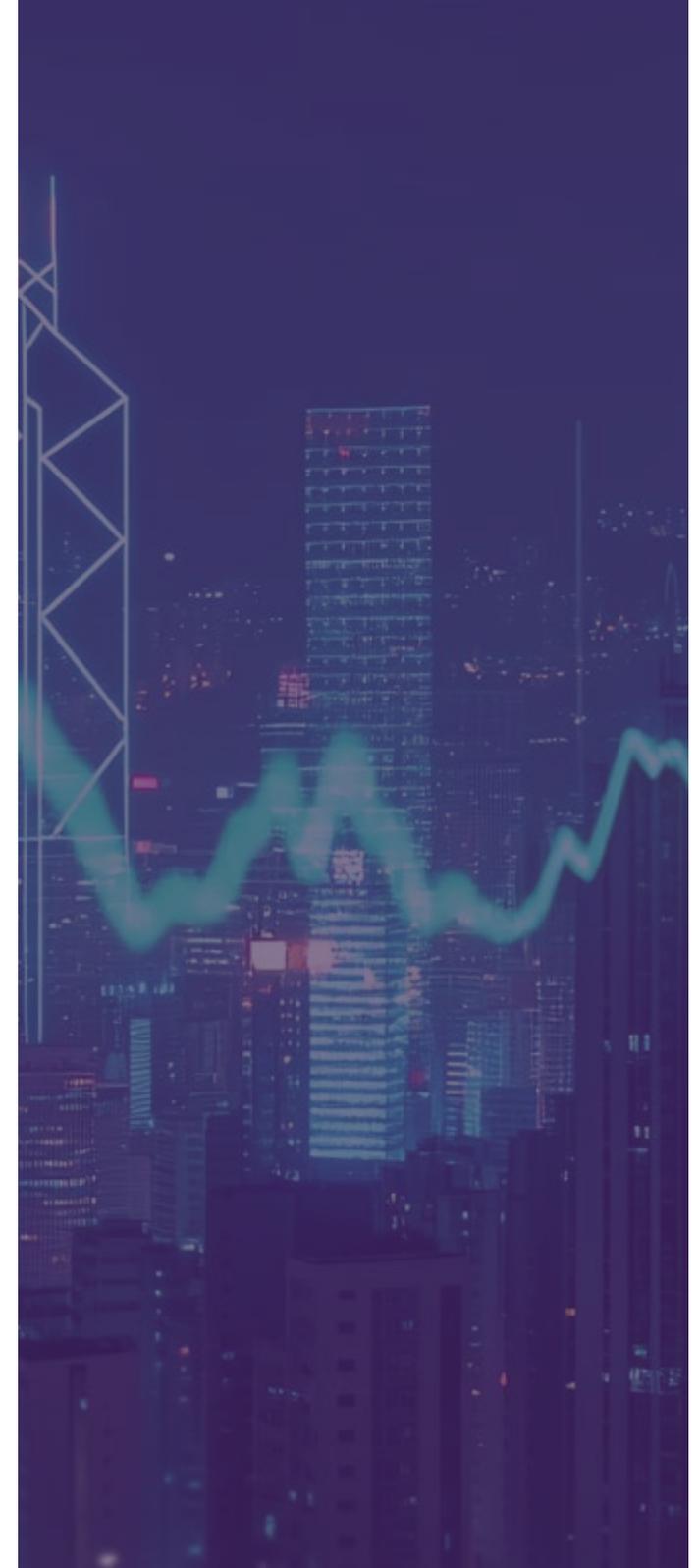
01 | Introduction

The lending market has markedly evolved in the last couple of decades. One of the most significant aspects has been the shift from originate-to-hold to originate-to-distribute (OTD) models. Whereas historically, lenders used to originate loans and hold them through maturity, several market factors have necessitated a diversification of risk.

Diversification of funds, optimisation of asset management, risk optimisation, as well as a need for increased profitability have catalysed the OTD model—particularly when banks retain the right to service the loans.

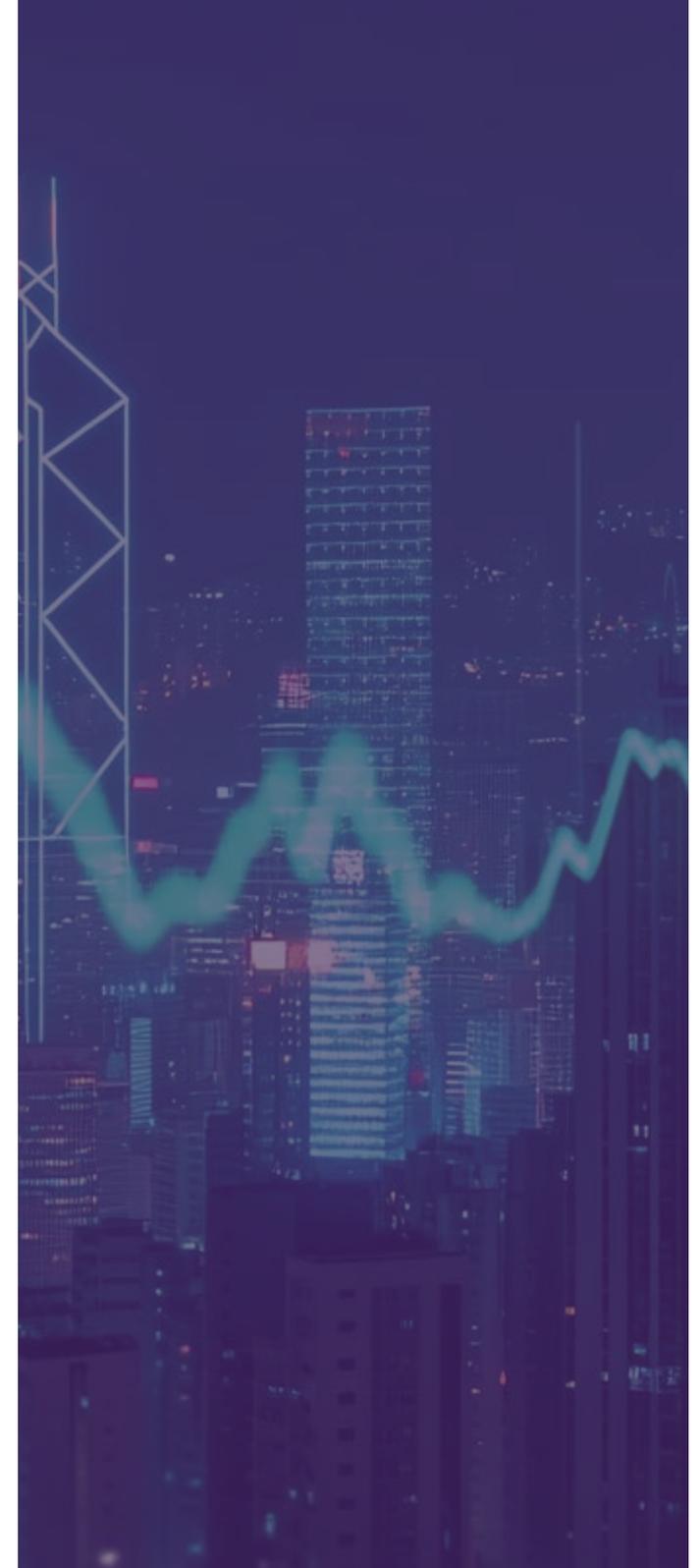
In recent years, as a result of the rising demand of collateralised loan obligations (CLOs), driven by the increased demand for corporate loans, the loan market has experienced spectacular growth. Research finds that the collateralised loan obligation market is expected to grow from \$1413.75 billion in 2024 to \$1615.41 billion in 2025.

The secondary loan trading market is experiencing similar growth. While the US market has been more mature and developed for years, first quarter trading volume in the secondary trading market reached a record \$253 billion in 2025, according to LSTA. While less liquid than the US, the European secondary trading market has seen similar growth spurts since banks have started to diversify—total transaction volume grew by 17% from 2023 to 2024.



However, barriers to adoption remain as banks grapple with infrastructure and data concerns, and regulatory updates in the space are further affecting how banks approach and optimise their OTD models. On top of that, increasing interest rates over the last four years have meant increased risk for banks that are already struggling with regulatory and capital cost. Add to this the rise of private credit institutions that offer direct lending (and face lower regulatory and capital cost), and banks are starting to feel the pressure of decreasing margins.

This impact study, produced in association with FIS, explores the challenges banks face in the lending space amidst increased competition, inadequate data structures, regulatory requirements, the growth of OTD models and the secondary loan trading market, and the opportunity that OTD models—combined with artificial intelligence (AI)—offer to help optimise banks' portfolios and balance sheets.

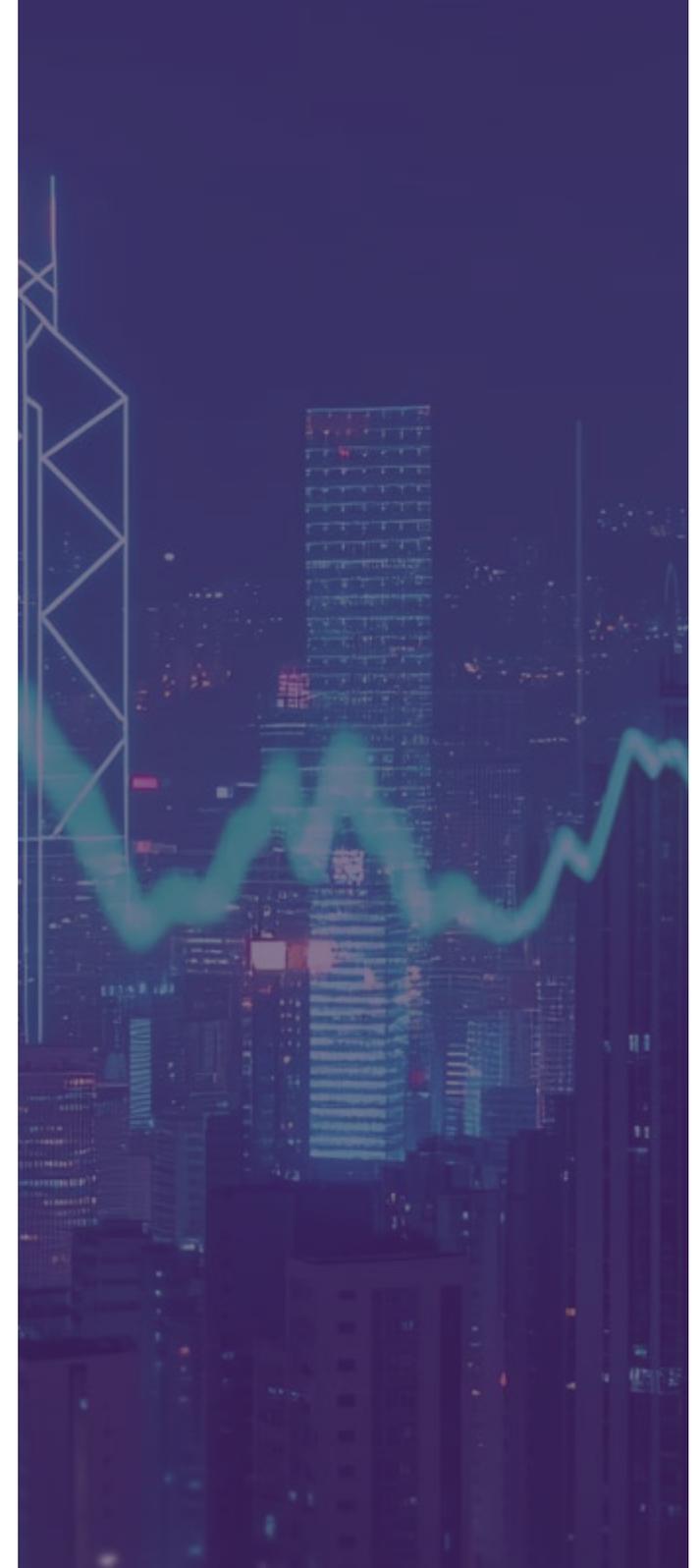


02 | Why lending has been increasingly challenging for banks

As the primary loan market evolves, incumbent banks are facing several challenges.

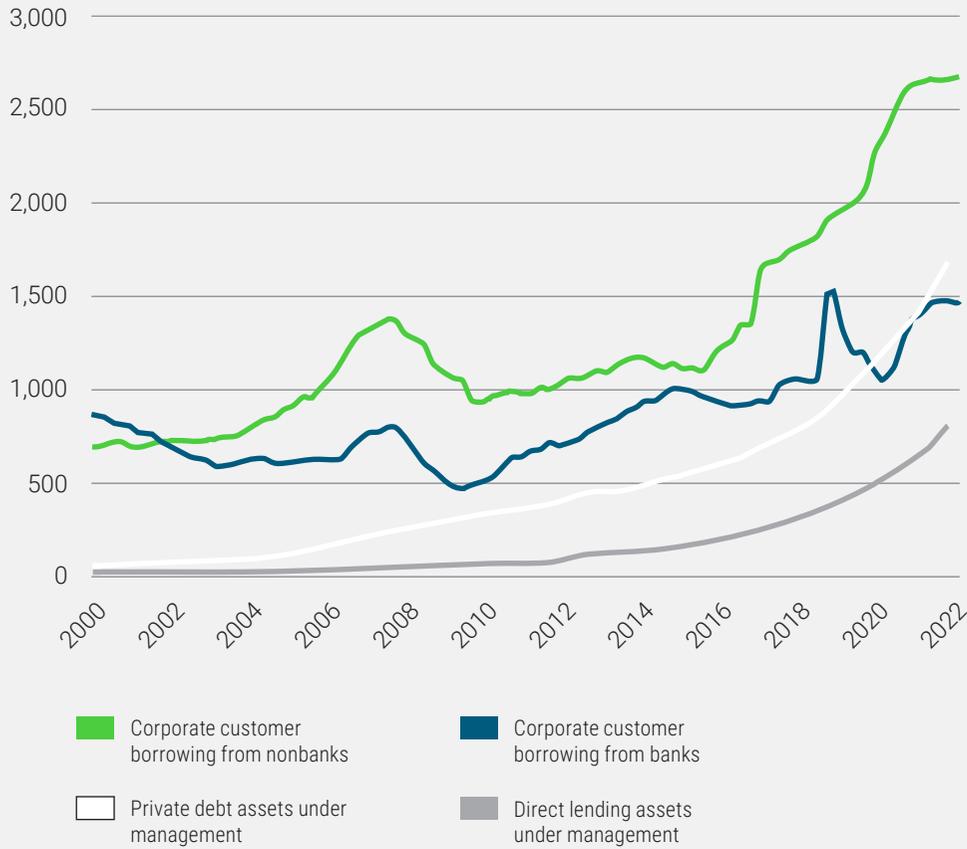
Increased competition through private credit

Private credit has been one of the fastest growing segments in the financial sector over the past decade, with McKinsey finding that private credit totalled almost \$2 trillion by the end of 2023. While private credit historically centred on direct lending, over the last few years, private lenders have increasingly diversified into a broader range of assets—such as commercial loans. Deloitte research, as illustrated below, highlighted that in the US alone, non-bank corporate borrowing grew tremendously since 2020, while bank borrowing fell from 44% in 2020 to 35% in 2023.



Bank vs private corporate borrowing in the US

Borrowing from banks and nonbanks, 2000 to 2023 (US\$ billion)



Source: [Deloitte](#)



There are several reasons private credit has flourished where banks have struggled. For one, non-bank lenders are generally not as challenged by infrastructure and data requirements as banks. While for banks, updating core infrastructure, systems, and processes can be complex, lengthy and expensive endeavours, private lenders often have more agility and flexibility in their operations. This can enable a more efficient lending process, and private credit firms are often able to offer more tailored solutions to their customers.

Secondly, as private credit firms are non-bank financial institutions, they face less regulatory and capital requirements compared to banks. As regulatory scrutiny increases, banks need to ensure compliance on several fronts. (Specific regulatory concerns are addressed in chapter 3.)

OTD models allow banks to originate loans, but sell them to private credit firms as opposed to holding them on their balance sheets. This strategy can be extremely beneficial to the overall risk management, however, in order to effectively optimise portfolios and determine which loans to hold onto and which loans to sell, banks don't just need the right data, but the right infrastructure. This leads us onto the next challenges.

Barriers to OTD adoption and other considerations

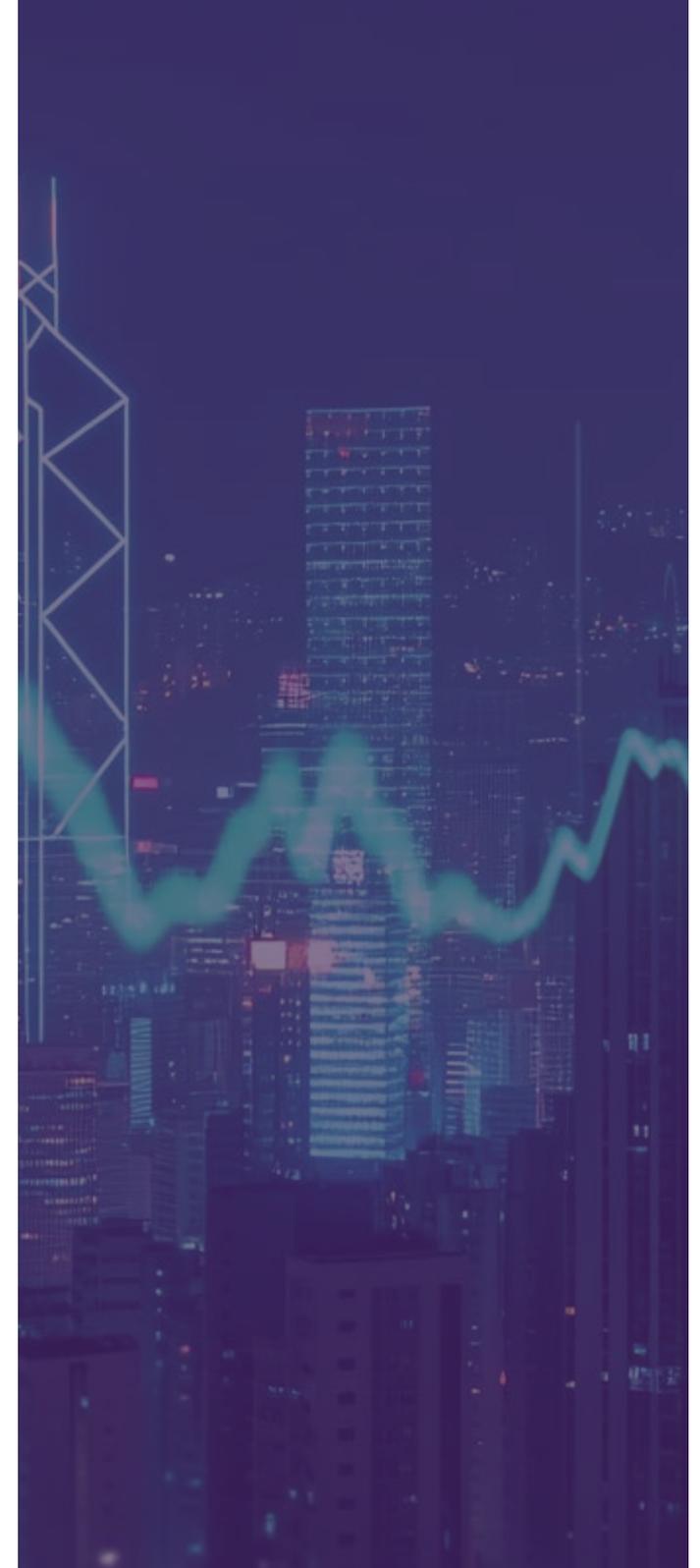
One of the major barriers to bank adoption of OTD models is the lack of internal infrastructure to support it, particularly when banks retain the rights to servicing the loans. Bank infrastructure can be highly complex and require significant investment for upkeep alone. [Data](#) from 2025 finds that 70% of IT budgets are spent on maintaining legacy systems, leaving little room for innovation. When teams have to manually address, manage, and service OTD loans, institutions may be forced to restrict volumes or incur higher staffing and error cost.



Private lenders often have more agility and flexibility in their operations – enabling a more efficient lending process and more tailored solutions than traditional banks.

Similarly, inadequate data structures can make it challenging to effectively analyse portfolios and determine which loans should be kept on balance sheets and which should be distributed. Dispersed data, particularly in origination platforms that can lack detail if based on a CRM platform, is a major barrier to adoption of a successful OTD strategy.

Looking at the value chain of a loan, distribution of loans needs consideration when it comes to reporting. Financial institutions have to adhere to the International Financial Reporting Standard (IFRS 9), and switching from an originate-to-hold to an originate-to-distribute model can add increased complexity to the reporting process.



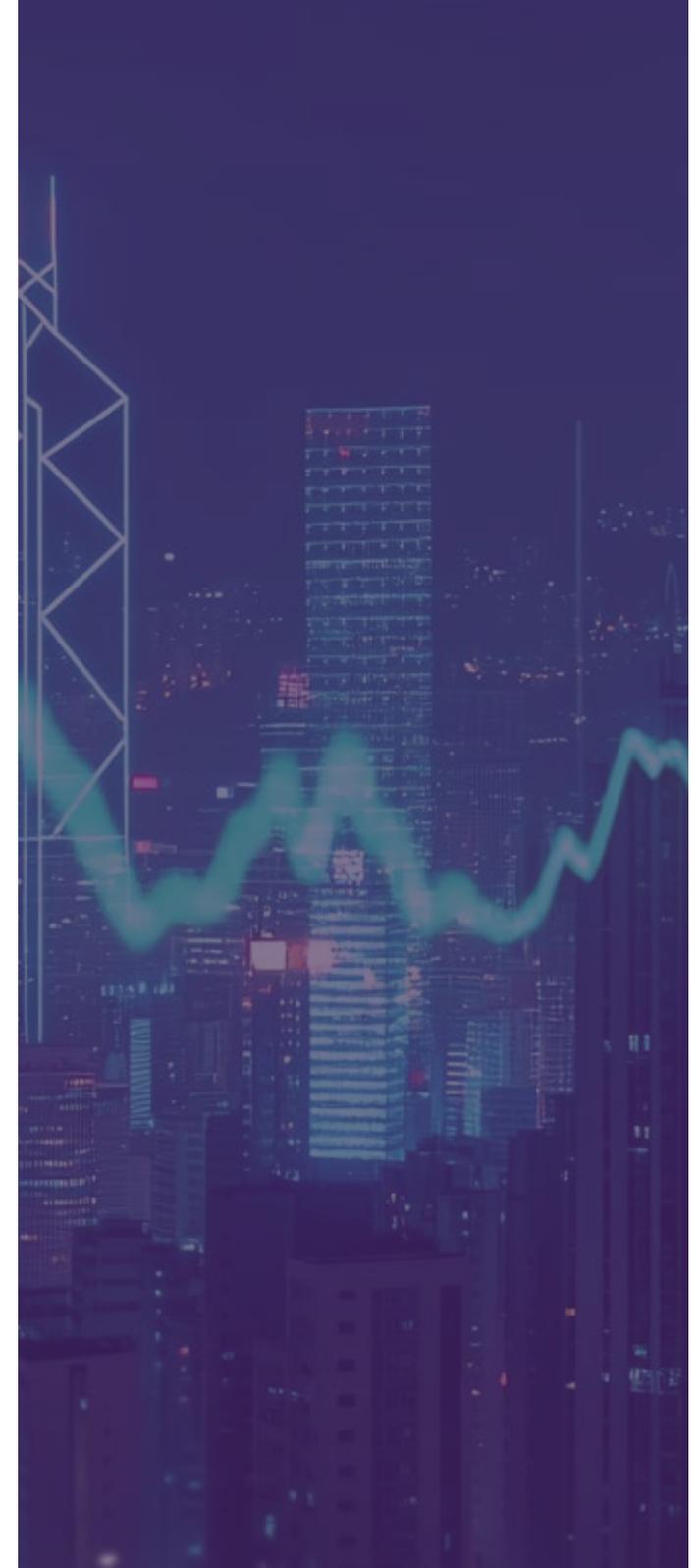
03 | Basel 3.1 and the impact of regulation

Increased regulation in the space—a direct response to the subprime mortgage crisis of 2008, caused by severe mismanagement of risk in the secondary loan trading market—is designed to cause lenders to more effectively manage their risk and retain enough capital to absorb potential losses in times of financial distress.

The main regulatory response, titled Basel III by the Basel Committee on Banking Supervision (BCBS), was first set out in 2010. Final changes and revised risk frameworks of Basel III were introduced in 2017 and 2019 and are yet to take full effect due to delayed deadlines. While these changes are part of Basel III reforms, they are also widely referred to as either Basel IV, Basel 3.1 (primarily in the UK), or Basel III Endgame (primarily in the US).

These reforms, which we will refer to as Basel 3.1, require banks to increase capital reserves in a variety of lending areas and include new liquidity requirements. These factors are likely to reduce banks' abilities to offer higher risk loans, reduce appetite to offer longer-duration loans, and lead to an increase in lending by less regulated entities—such as private credit firms.

As Basel 3.1 requirements are international standards, regional differences emerge as the standard affects each jurisdiction differently:



United States

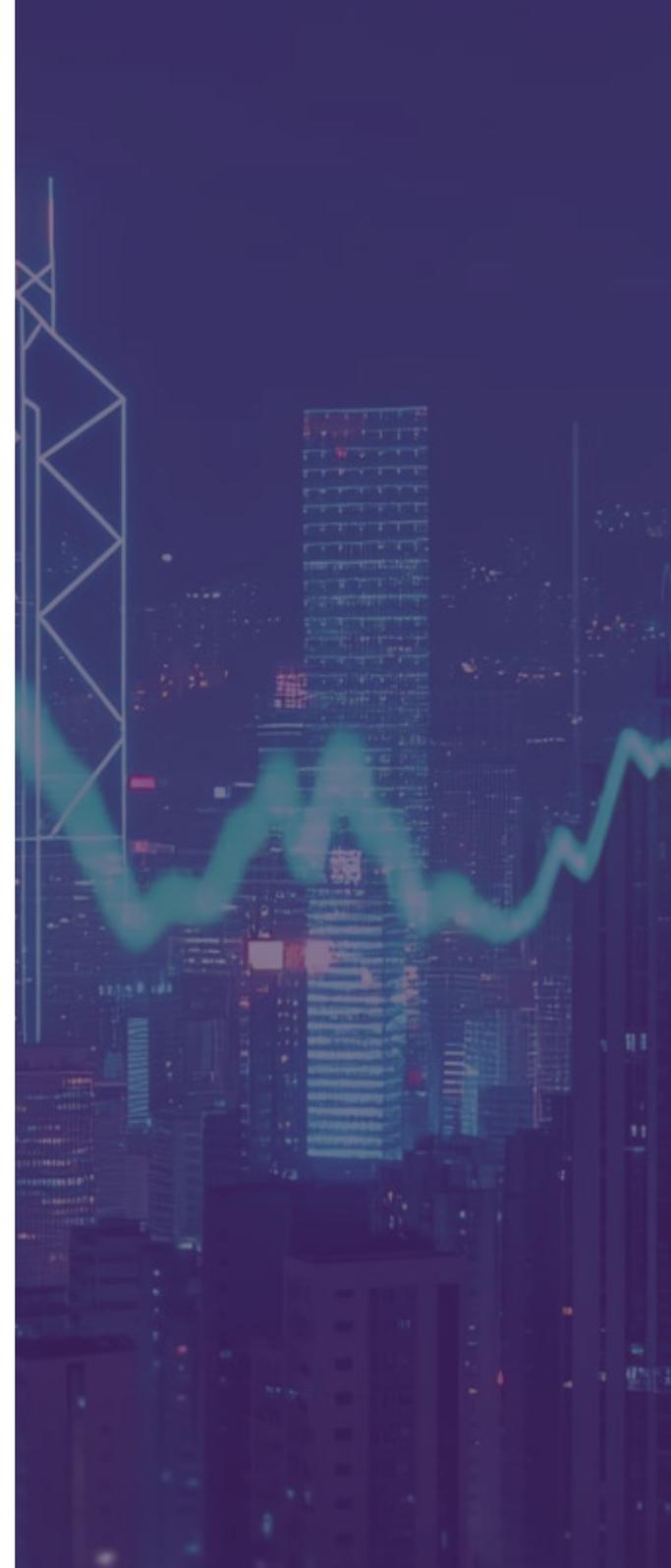
Referred to as Basel III Endgame in the US, the federal banking regulators initially proposed rules to implement the Basel reforms in July 2023. After months of extensive lobbying from the industry, the Federal Reserve loosened capital requirements of the proposed reforms in September 2024.

US reforms of Basel III have not been finalised and remain in doubt as the Trump administration historically favours de-regulation. Uncertainty about the final framework itself as well as timelines in the US are affecting implementation of Basel III reforms on an international scale.

United Kingdom

The UK's Prudential Regulation Authority (PRA) published the near-final policy statement regarding Basel 3.1 implementation in September 2024. Changes to the draft policy include, among others, amendments to the treatment of SME lending to reduce the operational burden for firms and lower capital requirements, amendments to the treatment of infrastructure lending to lower capital requirements, and approach to calculating the output floor which enhances consistency between standardised approaches and the output floor.

In January 2025, in consultation with HM Treasury, the PRA announced its decision to delay the implementation of Basel 3.1 in the UK until 1 January 2027. This delay is designed to allow for more time as the UK waits for greater clarity to emerge about Basel 3.1 implementation plans in the US. The PRA further stated that the transitional periods will be reduced to ensure the date of full implementation remains on 1 January 2030.

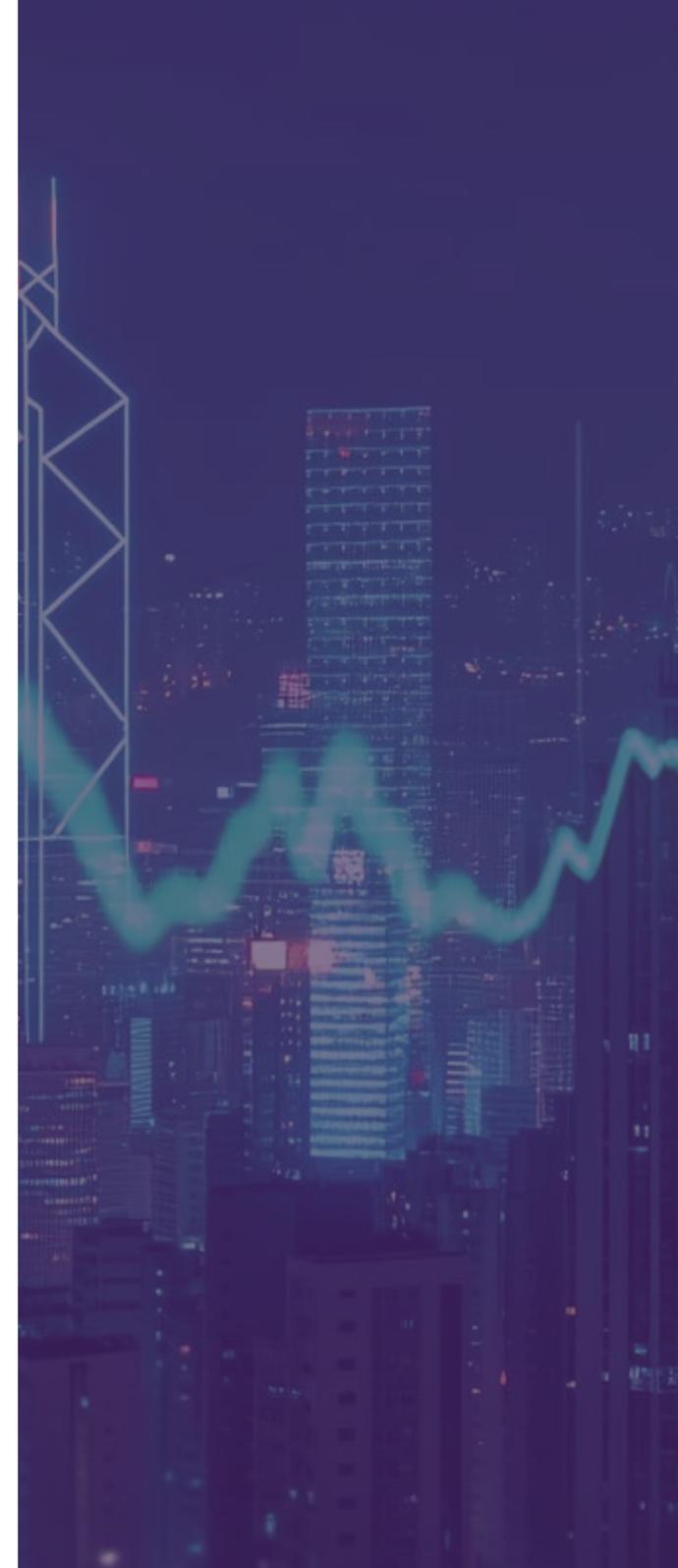


European Union

The Basel 3.1 framework is implemented in the EU via the “Banking Package”, which includes the Capital Requirements Regulation (CRR) III and the Capital Requirements Directive (CRD) IV. The final elements were agreed on and endorsed by the Council and Parliament in December 2023.

Some of the new CRR III rules were supposed to start applying on 1 January 2025, yet in light of the US delays, the EU has also decided to delay reforms by one year to January 2026 to allow for a more even global playing field. The CRD IV continues to be transposed by member states during its 18-month transposition period. The deadline for member states to implement CRD VI into national law is currently set for January 2026 as well.

Crucially, the regulatory shift still allows for both limit and capital relief if credit risk insurance is applied. The European Banking Authority writes: “Credit insurance, which is recognised as an unfunded credit protection (UFCP) as it shares the same economic nature as guarantees, is still expected to lead to a reduction of own funds requirements, albeit to a lesser degree than under the current framework.”

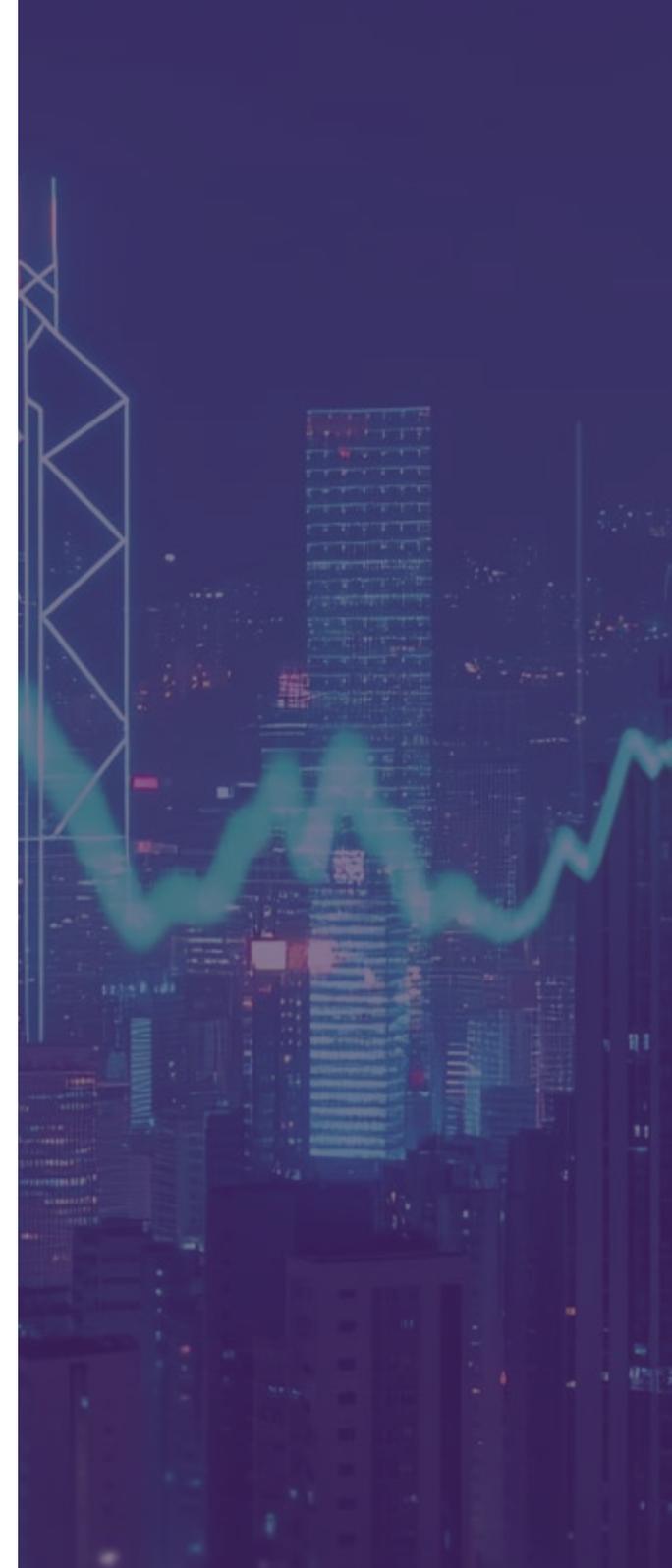


Credit insurance approach in the UK and EU:

- 1** Credit insurance remains eligible as a “guarantee” and therefore as unfunded credit protection for the purposes of CRR capital credit.
 - 2** The PRA are proposing to change this by removing the AIRB approach for risk weighting exposures to insurers (and other financial institutions) and crucially taking away the banks’ discretion to assess their recoverability.
 - 3** Rather, the banks will be required to adopt what’s called “prescribed FIRB LGDs” which means Foundation Internal Rating Based Loss Given Defaults.
 - 4** Under the PRA’s proposal: “the prescribed FIRB LGD for senior unsecured claims on an insurer would be 45%”, which would be the “lowest LGD that could be substituted in the case of an exposure with credit insurance”.
 - 5** Converting that into non-Basel 3.1 terminology, this means that banks will need to assume a maximum recoverability of 55% of the value of the credit insurance policy (but can assume less than 55%) for the purposes of capital credit.
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Source: [Simmons & Simmons](#)

The lack of a Clearing House to ensure trades across all counterparties adhere to the same behaviour and timelines is another consideration in this regard. When it comes to risk management, associating hedging strategies like non-payment insurances (NPI) and credit default swaps (CDS) with individual positions is challenging. In Europe specifically there is no standardised pricing for broadly syndicated loans (BSL), which necessitates the use of mechanisms like fair-value spreads (FVS) to determine a benchmark price of such credits.

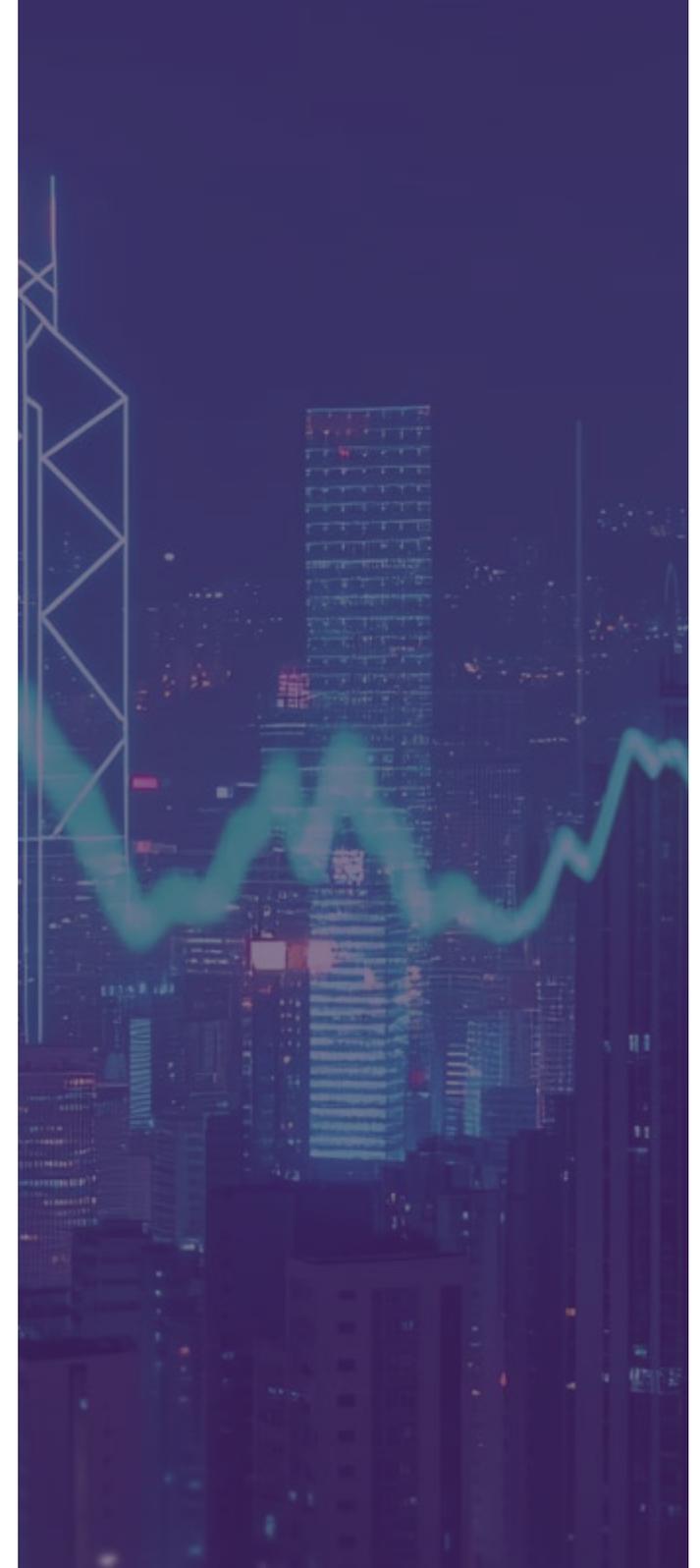


04 | Opportunities of OTD models and implications of AI

Deloitte found that “many banks are not embracing new opportunities, even when private credit poses a serious risk to their current lending business.” OTD models can offer just such an opportunity if banks are willing to invest the time and effort to negate the barriers of adoption discussed earlier.

Particularly considering the upcoming Basel 3.1 requirements, Deloitte writes that OTD models and relationships between banks and private credit can be beneficial to both entities: “Corporate clients may benefit from faster and more flexible lending terms while private credit firms benefit from the bank’s relationships. For banks, one advantage of working with private credit firms is retaining less credit risk. With the expected adoption of Basel III endgame capital requirements, banks may be limited in their ability to lend to riskier clients. But since private credit firms are non-banks, they often face fewer regulations. Working in partnership may help banks provide better service to their corporate borrowers.”

McKinsey additionally recommends that banks “move the final ownership of those loans through several mechanisms, including expanding traditional syndication capabilities to a broader set of investors, using forward-flow agreements, emphasising asset sales, pursuing synthetic risk transfer trades, and even creating asset management vehicles in partnership with private credit companies. In doing so, they could become originators and distributors rather than end owners of risk.”



Crucially, in order to be able to do all of this as well as optimise their margins, banks can leverage advanced AI to start accelerating how they look at their portfolios of loans—both when originating and closing transactions, but also their existing on-balance-sheet portfolios—and help to identify the right assets and cashflows to distribute.

- **Automation** helps standardise lending processes and remove the manual input and time necessary to issue credit decisions.
- **Alternative data sources** can complement traditional data in order to improve pricing and risk algorithms.
- **Machine learning and AI** can help banks improve underwriting decisions and more effective portfolio monitoring.

Apart from the origination of loans, AI and machine learning technologies can also help banks better prepare loans for the secondary market. Traditionally, lenders had to rely on manual quality assurance from post-closing departments to ensure loans sold on the secondary market meet regulatory demands as well as expectations of risk-averse investors.

AI-backed technology helps banks spread these quality assurance tasks throughout the loan life cycle, which can significantly reduce the risk of inaccuracies, non-compliance, non-saleability, and cost of errors. When managed in a cohesive solution, this allows for a permanent association between loan data and source documents, helping to make it easier to trace and correct inaccuracies as and when they occur.

As these AI technologies mature and banks continue to develop the use cases around them, a future is not far-fetched where a generative AI tool can propose the most opportune distribution opportunities and give advice on balance sheet strategy.



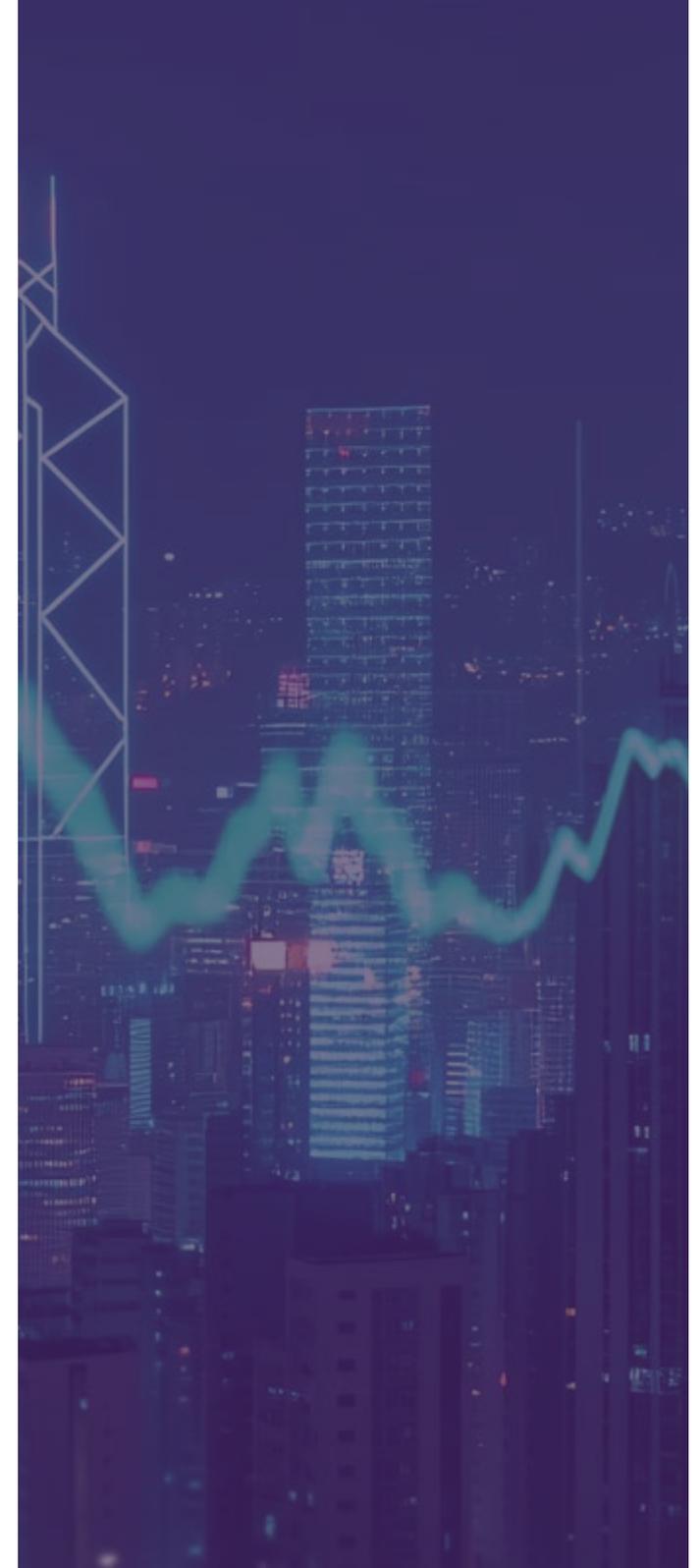
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05 | Conclusion

Increased competition, lower margins, and growing regulatory scrutiny are pushing banks to re-think their lending strategies. OTD models allow banks to do just that—boost liquidity while diversifying risk.

However, a major challenge banks continue face with diversification is inadequate data structures to optimise their balance sheet and determine which loans should be distributed to maximise the benefit to the organisation. Effective screening, monitoring, and assessment are critical as the popularity of OTD models grows—yet too much data remains in silos.

AI and machine learning technologies can help banks modernise decades-old processes, eliminate siloes, and improve their decision-making. The time is now to start developing the use cases around AI or risk the cost of passivity.



06 | About

Finextra Research

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