

RMBS/Spain  
New Issue

## Bankinter 7, Fondo de Titulización Hipotecaria

### Ratings

Class	Amount (EURm)	Final Maturity	Rating	CE (%)
A	471.8	Sept 2040	AAA	5.20
B	13	Sept 2040	A	2.55
C	5.2	Sept 2040	BBB	1.50

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### ■ Summary

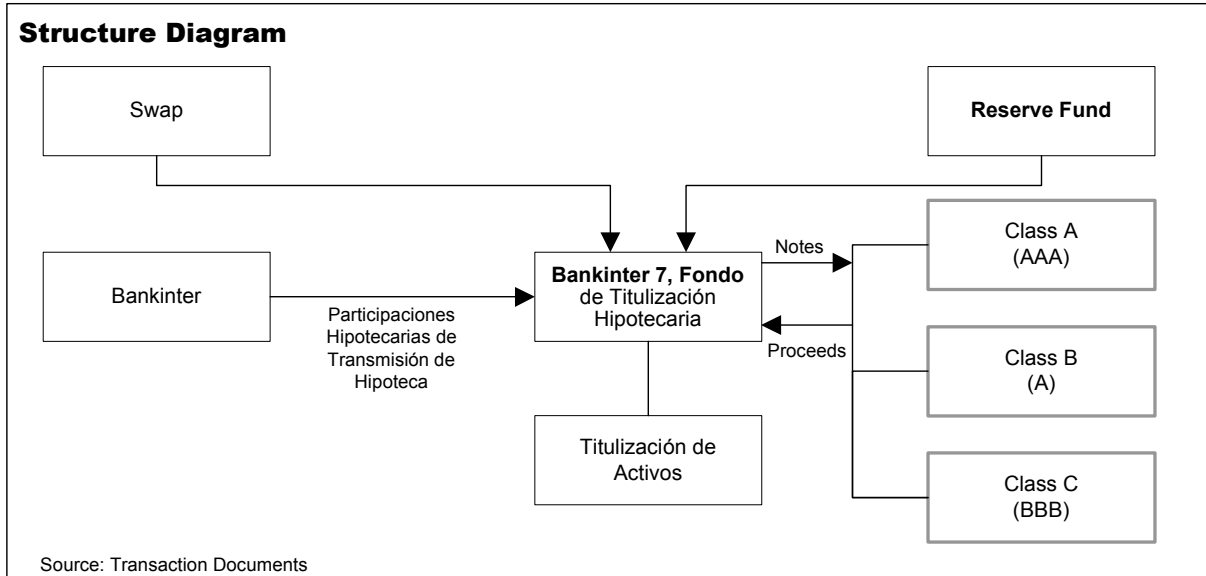
This EUR490million transaction is a securitisation of 5,275 residential mortgage loans originated in, and secured on, property located in Spain. Fitch Ratings has assigned ratings to the notes to be issued by Bankinter 7, Fondo de Titulización Hipotecaria (“Bankinter 7” or “the fund”) as indicated at left.

At closing, Bankinter 7 issued notes backed by a portfolio of residential mortgage loans originated by Bankinter S.A. (“Bankinter” or “the seller”). The latter will continue servicing the loans. Bankinter 7 is regulated by Spanish Securitisation Law 19/1992 and Royal decree 926/1998. Its sole purpose is to transform the mortgage loan participations acquired from the participation issuer, Bankinter, into variable rate residential mortgage backed securities (“RMBS”). The participations were subscribed on behalf of Bankinter 7 by Europea de Titulización, S.A., S.G.F.T. (“the *Sociedad Gestora*”), whose sole function is managing asset-backed funds.

Bankinter is one of Spain’s largest financial institutions, created in 1965 by Santander and Bank of America. Securitisation is an important tool in its financing strategy. Indeed, the bank has issued in the past few years a number of securitisation transactions, among which six RMBS and one SME CDO. Its business has developed since its inception to become more consumer oriented; it has in fact focused on the Spanish residential mortgage market, with a current market share of around 8%.

The ratings are based on the quality of the collateral, the underwriting and servicing of the mortgage loans, available credit enhancement and the sound legal and financial structures. Initial credit enhancement for the Class A notes, totalling 5.20%, is provided by the subordination of the Class B notes (2.65%) and the Class C notes (1.05%) and an initial reserve fund (1.5%). Initial credit enhancement for the Class B notes is 2.55%, provided by the Class C notes and the reserve fund. Initial credit enhancement for the Class C notes is 1.50%, provided by the reserve fund.

To determine appropriate levels of credit enhancement, Fitch analysed the collateral using a loan-by-loan mortgage default model specific to Spain. The agency also modelled the cash flow contribution from excess interest using stress scenarios determined by its default model. The cash flow test showed that each class of rated notes, taking available credit enhancement into account, could withstand loan losses at a level corresponding to the related stress scenario without incurring any principal loss or interest shortfall, according to the terms and conditions of the notes.



## ■ Credit Committee Highlights

- Unlike some other Spanish transactions, debt to income (“DTI”) information was provided on a loan-by-loan basis. Around 46% of the pool was in Fitch’s DTI class 3, the remainder was in lower DTI classes.
- Seasoning is around 33.2 months, which contributed to a lower weighted average indexed current loan-to-value (“LTV”) of 64.8% compared with a current weighted average LTV of 73.7%.
- The hedging mechanism in place mitigates the risk of differences between the mortgages’ and the notes’ indices.
- The expected ratings address payment of interest on the notes according to the terms and conditions of the documentation, subject to a deferral trigger for the Class B and Class C notes, as well as the repayment of principal at final maturity.

## ■ Financial Structure

Interest on the notes will be paid quarterly in arrears based on three-month EURIBOR plus a margin.

The mortgages will continue to be serviced by Bankinter, acting as the administrator. Amounts received from the mortgages will be transferred by the bank into the fund’s GIC (Guaranteed Investment Contract) account, held at Bankinter, on a weekly basis. As Fitch does not rate Bankinter but requires that the fund’s account be held by an ‘F1’ rated bank, the agency will monitor the financial situation of the bank and advise the *Sociedad Gestora* if it deems

that the account should be transferred to another ‘F1’ rated bank.

The legal maturity of the notes is September 2040. The notes are subject to a clean-up call when less than 10% of the mortgage participations at closing remain outstanding.

The mortgage loans will continue to be serviced by Bankinter. However, in the event that it is unable to perform this function adequately, the *Sociedad Gestora* will appoint a replacement administration company in accordance with Law 19/1992, subject to rating agency confirmation.

## Priority of Payments

On each distribution date, revenue payments will be allocated in the following order of priority:

- senior fees and expenses;
- payments due under the interest rate swap agreement;
- interest due on the Class A notes;
- interest due on the Class B notes, if not deferred;
- interest due on the Class C notes, if not deferred;
- principal due on the notes;
- interest due on the Class B notes, if deferred;
- interest due on the Class C notes, if deferred;
- replenishment of the reserve fund;
- payments due under the swap in the event of a swap counterparty default, if any;
- interest due on the loan for initial expenses;
- amortisation of the loan for initial expenses;
- interest due on the subordinated loan;
- amortisation of the subordinated loan;
- payments due to the loan administrator if the latter is Bankinter;
- variable remuneration on the subordinated loan.

## Key Information

### Provisional Portfolio Characteristics

**Total Amount at Closing:** EUR490m

**WA Original LTV:** 80.4%

**WA Current LTV:** 73.7%

**WA Indexed Current LTV:** 64.8%

**WA Remaining Maturity:** 24.11 years

**WA Seasoning:** 33.2 months

### Structure

**Originator & Seller:** Bankinter S.A. (Bankinter)

**Servicer:** Bankinter

**Fund:** Bankinter 7, Fondo de Titulización Hipotecaria (Bankinter 7)

**Sociedad gestora:** Europea de Titulización, S.A., S.G.F.T.

**Swap Counterparty:** Bankinter

**Final Legal Maturity:** September 2040

Interest due on the Class B notes will be deferred if the amortisation deficit exceeds 50% of the initial Class B note balance and 100% of the initial Class C note balance. Deferral of the Class B notes is subject to the Class A notes remaining outstanding.

Interest due on the Class C notes will be deferred if the amortisation deficit exceeds 50% of the initial Class C note balance. Deferral of the Class C notes is subject to the Class A and Class B notes remaining outstanding.

The amortisation deficit is the difference between 1) the current balance of the notes and 2) the current balance of the loans excluding losses. The latter are defined as mortgages more than 18 months in arrears.

In the event that the fund needs to be liquidated, the notes will become due and payable. All available funds will then be allocated sequentially to cover interest and principal payments due on the Class A notes, then the Class B notes and finally the Class C notes.

### Principal Redemption

The principal payments due on the notes will be allocated sequentially, starting with the Class A notes then the Class B notes and finally the Class C notes.

However, the notes can be amortised in a *pro rata* manner if the Class B and Class C notes represent twice the credit enhancement that they did at closing,

ie 5.3% and 2.1%, respectively. Moreover, *pro rata* amortisation can only take place subject to the following conditions:

- The reserve fund is at its maximum level;
- There is no amortisation deficit; and
- The current balance of loans more than 90 days in arrears, excluding losses, is less than 1.5% of the outstanding balance of the loans, excluding losses.

### Interest Rate Risk

The fund will enter into an interest hedging agreement with Bankinter to cover the risk of the difference between the indices on the mortgages and that of the notes.

Hence, the fund will pay Bankinter the index received from the mortgages less than 18 months in arrears and will receive from the swap counterparty three-month EURIBOR on the notional balance of the notes. No excess margin is guaranteed.

Fitch does not rate Bankinter as a swap counterparty. However, it will monitor the financial situation of the bank, and, will advise the *Sociedad Gestora* if it deems that Bankinter as a swap counterparty should be replaced to avoid it having a negative impact on the rating of the notes. If Bankinter is replaced by another entity, and in the event the latter's short-term rating is downgraded below 'F1', it will, within 10 days, complete one of the following:

- cash or security collateralise its obligations for an amount satisfactory to the agency;
- find a replacement counterparty with a short-term rating of at least 'F1'; or
- find an entity rated at least 'F1' to guarantee its obligations under the swap.

### Credit Enhancement

Initial credit enhancement for the Class A notes, totalling 5.2%, is provided by the subordination of the Class B notes (2.65%), the Class C notes (1.05%) and an initial reserve fund (1.50%). Initial credit enhancement for the Class B notes is 2.55%, provided by the Class C notes and the reserve fund, whereas initial credit enhancement for the Class C notes is 1.50%, provided by the reserve fund.

### Reserve Fund

The reserve fund at closing will equate to 1.5% of the initial notes' balance. Subject to the following conditions, it will be permitted to amortise to the lesser of: a) 1.5% of the initial notes' balance or b) 3% of the then outstanding notes' balance:

- the balance of mortgages loans more than 90 days in arrears remains below 1% of the outstanding mortgage balance;
- there is no amortisation deficit; and
- the outstanding balance of mortgages is at least 10% of the initial balance.

The reserve fund will be subject to a floor of 1% of the original note balance at all times.

### Representations and Warranties

Bankinter will provide representations and warranties in relation to the pool of mortgages, a breach of which will result in Bankinter repurchasing the loan(s) in question.

Specifically, the representations and warranties include the following, amongst others:

- each mortgage loan is registered in the relevant property registry and is first-ranking on its corresponding property;
- Bankinter has full right and title to, and the power to sell and transfer, the mortgages;
- Bankinter is unaware that any of the underlying properties have been subject to more than a 20% reduction in value;
- all properties are located in Spain;
- each property under the underlying mortgage loan has been the subject of a valuation as required by law; and,
- each mortgage loan constitutes legal, valid, binding and enforceable obligations of the relevant borrower.

### ■ Legal Structure

At closing, the mortgage loans will be transferred by Bankinter to the *Sociedad Gestora* on behalf of the fund. The seller will also transfer all present or future rights under the various transaction documents to the fund. The *Sociedad Gestora* is a special purpose company with limited liability incorporated under Spanish laws. Its activities are limited to the management of asset-backed notes.

Mortgages with current LTVs below 80% are transferred to the fund as mortgage participations (*P participaciones Hipotecarias*), and, as per recent changes in legislation, all others are transferred to the fund as certificates of mortgage transfers (*Certificados de Transmisión Hipotecaria*).

### Collateral

The provisional reference portfolio consists of 5,275 mortgage loans originated by Bankinter. All are secured by residential properties in Spain and benefit from first-ranking mortgages registered in the

“*Registro de la Propiedad*” (the Spanish official register).

All the loans are variable-rate, linked to EURIBOR/MIBOR. No large geographical concentration exists in this portfolio. The regions with the largest percentages of loans are Madrid and Catalonia, with 25.1% and 17.1% of the pool, respectively, which is more or less consistent with the breakdown of the population.

Income information was available on a loan-by-loan basis. Some 45.7% of the pool had a DTI in Fitch’s class 3, with the remainder in lower classes of DTI. The majority of the portfolio has original LTVs between 70% and 90%, with a weighted average original LTV of 80.4%. Seasoning is around 33.2 months, which has caused a significant decrease in the current LTV of 73.7% to an indexed current LTV of 64.8%. The largest current LTV in the pool is 80%.

The majority of mortgages were taken out on the borrowers’ first residence, and the remainder on second homes (3.8%). Although limited information was available on their employment status, less than 11% were self-employed or in temporary employment.

The average property price was approximately EUR131,000 (on a weighted average basis), and no property price exceeded EUR500,000. Nevertheless, Fitch applied a jumbo hit (see below) to more than 8% of the pool.

### ■ Origination and Servicing

Bankinter, S.A. (Bankinter) was created in 1965 by Santander and Bank of America, becoming independent in 1972, and is today the sixth largest bank. Bankinter’s strategy has changed to focus more on the retail sector, which has become a much larger portion of the bank’s balance sheet, and today accounts for more than 42% of its activities, among which the largest is mortgage lending.

The bank has, in recent years, decided to concentrate on a specific segment of customers, those with above average income, with an average age of 30-40 years. On average, the bank has 5.7 products per client, while the market average is around 3 or 4 products per client.

Although the bank has reported strong growth in its mortgage origination, defaults have remained lower than the rest of the market, 0.154% compared with a market average of 0.41% (calculated as loans 90 days in arrears as a proportion of the outstanding mortgage loan balance).

## Origination

Mortgages are originated through the bank's branches, telephone banking, internet and a real estate network of estate agencies. Information required for origination includes, among others, information on a borrower's family situation, employment situation, other sources of revenue, history with the bank, total debts outstanding, a valuation of the underlying property by one of Bankinter's accepted valuers, which are all Bank of Spain's registered and regulated valuation companies. The bank will consult with its own internal customer databases as well as external credit sources, such as ASNEF, CIRBE (which keeps records on default history and current debt exposures). Its internal credit system is based on the capacity of the borrower to repay its debt. The large majority of mortgages loans are approved through this system. Manual approvals do exist, however, but have restrictive loan amounts, LTVs and DTI limits, depending on the seniority of the approving credit officer.

**LTVs:** Mortgages on a borrower's main residence are limited to 80%, with some exceptions. While loans on second homes are limited to a LTV of 60%.

**DTI:** Although DTI is limited to 40% (with some exceptions), the bank aims to keep the ratio at less than 35%. This ratio is calculated using net (declared) income.

## Provisional Portfolio Summary

### Pool Characteristics

Current Principal Balance (EURm)	509.4
Average Current Loan per Borrower (EUR)	96,575
Average Original Loan per Borrower (EUR)	105,479
Oldest Loan in Portfolio	March 1997
Most Recent Loan in Portfolio	March 2003

### Interest Rate Type

Floating Rate Loans (%)	100
WA Interest Margin (%)	0.66
Interest Index	EURIBOR, MIBOR

### Payments

Payment Frequency (%)	Monthly: 100
Payment Method	Direct Debit
Loans <30 Days in Arrears (%)	98.73

### Regional Concentration (%)

Madrid	25.1
Catalonia	17.1

### Lien Position (%)

First-Ranking	100
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Source: Fitch Ratings

**Current Account:** The bank requests the borrower to keep its current account at Bankinter. Although it can not impose this, the majority do follow this rule.

## Servicing

As soon as a loan is more than one day overdue it is passed to the delinquencies and defaults department (D+D), where a credit officer decides whether to use an external telephone recovery agency, or to commence a more serious recovery process, ie by mail, and if necessary, legal proceedings. Simultaneously, other actions will be taken internally on other products that the customer will have with the bank (ie the blocking of his accounts etc).

The bank uses an external telephone recovery agency for those loans expected to remain at the delinquency stage. A standard set of telephone calls are programmed and, if necessary, personal visits. The bank also employs external legal counsel for all legal proceedings. The latter prepare all required documentation and organise the foreclosure process. They have to revert, however, to Bankinter for all business decisions. Moreover, they are obliged to provide regular updates.

The majority of delinquent loans are overdue owing to temporary financial difficulties. However, where the financial situation of the borrower is such that he will not be in a position to repay its debt, he will most often organise the sale of the property to avoid going to court. It is important to note that the bank will not abandon the legal process once it has started, unless the entire amount due is paid – or a large part of it. Hence, though the actual legal process lasts on average one to two years, and can last up to three years (fairly infrequent in the last decade), the large majority of recoveries tend to be in the first eight months.

Bankinter uses a system of alerts to identify potential delinquent borrowers. The system will use external credit databases, which will identify defaults on other financial institutions as well as important changes in the debt structure of the borrower. An internal database will track and flag abnormal changes.

## ■ Credit Analysis

Fitch analysed the collateral for this transaction by subjecting the mortgage loans to stresses resulting from its assessments of defaults of mortgage loans and movements of historical house prices in Spain. The analysis was based on default probability and expected recoveries on individual loans (see Appendix 1). To evaluate the contribution of structural elements such as excess spread, subordination, deferral triggers and other factors,

Fitch modelled the cash flows based on the weighted average (“WA”) frequency of foreclosure and WA recovery rate provided by the loan-by-loan collateral analysis (see A Guide to European RMBS Cash Flow Analysis dated 20 December 2002, available at [www.fitchratings.com](http://www.fitchratings.com)).

## Default Probability

Generally, the two key determinants of default probability are the willingness and ability of a borrower to make the mortgage payments. Willingness to pay is usually measured by the LTV ratio. Fitch assumed higher default probabilities for high LTV loans and lower default probabilities for low LTV loans, as in a severe negative equity situation borrowers in financial distress, but with equity in their homes (low LTV loans), have an incentive to sell and maintain/protect their equity, eliminating the need for the lender to repossess the property.

Ability to pay is usually measured by the borrower’s net income in relation to the mortgage payment. Bankinter is largely focused on a borrower’s ability to pay; it has comparatively strict origination guidelines in this area, and only allows a maximum DTI of 40%.

Fitch takes into consideration the specific characteristics of the product in the default probability analysis of the portfolio, taking the LTV based on the original balance of the initial drawdown as the main measure of a borrower’s willingness to pay.

## Recoveries

To estimate recoveries on the mortgage loans, Fitch examined house price movements in Spain on a regional basis from 1987-2003 and found significant differences, most notably between Madrid, Catalonia and the Basque Country and the other regions. Cities in these three regions have experienced higher price increases than elsewhere in Spain. Based on its analysis of the real estate market, Fitch assumed marginally larger market value declines (“MVDs”) for certain regions as well as for some large urban areas. Although price growth was stable in the period examined, it was slower in the regions of Valencia and Murcia. However, MVDs for these regions have tended to be lower than for the more populated areas of Spain such as Madrid and Catalonia.

Fitch has increased MVDs for higher value properties. These are generally subject to greater MVDs in a deteriorating market than homes with average or below-average market values for reasons of limited demand. Approximately 8.5% of the

reference pool is considered by Fitch to be secured on high value (“jumbo”) properties.

When calculating recovery values, Fitch’s model reduces each property’s worth by the MVD, external foreclosure expenses and the cost to the servicer of carrying the loan from delinquency through to default. The carrying cost will depend on the time to foreclosure as well as the interest rate applied, which Fitch assumes to be 5%. Bankinter’s current time to foreclosure is eight months, but Fitch assumed a figure of three years.

## Cash Flow Analysis

To evaluate the contribution of structural elements such as excess spread, reserve fund and other factors, Fitch modelled the WA cumulative frequency of foreclosure and WA recovery rate provided by the loan-by-loan collateral analysis to determine cash flows generated by the mortgages. Recoveries included both interest and principal.

The cash flow model assumes that defaults are spread over the first five years of origination immediately following closing. The analysis simulates the cost of carrying defaulted loans as the difference between the performing balance of the mortgages and the notional note balance. Excess spread, the reserve fund and principal must be sufficient to cover the carrying cost until recoveries are received after the assumed 36 months. Variable interest rates due on the notes are stressed upwards over time. However, the effect of the latter is limited owing to the basis swap in place.

The cash flow analysis assumes a high level of prepayments on the mortgages, which stresses available excess spread, of 25%, 21% and 18% *per annum* under ‘AAA’, ‘A’ and ‘BBB’ scenarios respectively.

Under these stresses, the payment of principal will be received before the final legal maturity date. The payment of interest will be received without interruption for the Class A notes. However, in the case of the Class B and Class C notes, this will be subject to the deferral trigger and the terms and conditions of the notes. Class B and Class C notes may, during a period of time, not receive any interest if the deferral triggers are hit.

## ■ Performance Analytics

Fitch will monitor the transaction on a regular basis and as warranted by events. Its structured finance surveillance team ensures that the assigned ratings remain, in the agency’s view, an appropriate reflection of the issued notes’ credit risk.

Details of the transaction's performance are available to subscribers at [www.fitchresearch.com](http://www.fitchresearch.com). Further information on this service is accessible at [www.fitchratings.com](http://www.fitchratings.com).

**Appendix I: Rating Methodology**

To determine appropriate levels of credit enhancement, Fitch analyses the collateral for Spanish residential transactions using a loan-by-loan mortgage default model. The model subjects the mortgage loans to stresses resulting from its assessments of historical house price movements and defaults. Fitch's study showed that the LTV, reflecting the size of the borrower's down payment, and the borrower's income multiple (original loan advanced divided by income) are the primary indicators of default risk in Spain. Fitch also modelled the cash flow contribution from excess interest using stress scenarios determined by its default model. The cash flow test showed that each class of rated notes, taking available credit enhancement into account, can withstand loan losses at a level corresponding to the related stress scenario without incurring any principal loss or interest shortfall.

**Default Probability**

Generally, the two key determinants of default probability are the borrower's willingness and ability to make the mortgage payments. The willingness of a borrower to pay is usually measured by the LTV. Fitch's model assumes higher default probabilities for high LTV loans and lower default probabilities for low LTV loans. The main reason is that in a severe negative equity situation, borrowers in financial distress but with equity in their homes (low LTV loans) have an incentive to sell and maintain/protect their equity, eliminating the need for the lender to repossess the property.

The ability to pay is usually measured by the borrower's net income in relation to the mortgage payment. Historical data available for Spain show low levels of default. Base default probabilities are determined using a matrix which considers each loan's affordability factor and LTV. The matrix classifies affordability into five classes, the lowest of which (Class 1) encompasses loans with debt-to-income ratios (DTI) of less than 20% and the highest of which (Class 5) encompasses all loans with DTIs exceeding 50%. The average DTI for the mortgage market in Spain is c. 27%-33%.

**Adjustments**

Fitch adjusts the base default rates on a loan-by-loan basis to account for individual loan characteristics of the collateral across all rating levels.

- **Product Type:** Fitch increases default probability assumptions by 0%-10% for the index volatility experienced by variable-rate mortgage holders.
- **Repayment Type:** Fitch will increase base default rates by 5%-10% for loans to be paid by *cuota creciente*, whereby the amortisation of capital is always the same and the interest payment is increasing.
- **Loan Purpose:** Fitch believes that a financially distressed borrower is more likely to default on a second home or investment property than on a primary residence. Accordingly, Fitch will double the base default rates in both cases. If the purpose of the loan is not to acquire a property in Spain, Fitch will increase the default probability by 50%-100%.
- **Borrower Profile:** Fitch increases default probability on loans to self-employed borrowers by 33%-50% to account for their lack of fixed annual salary.
- **Arrears Status:** when rating portfolios combining current and arrears mortgages, Fitch increases base default rates for mortgages in arrears by 1-30, 31-60, and 61-90 days by 10%, 35% and 70% respectively, and mortgages over 91 days in arrears (non-performing status) by 100%.
- **Underwriting Quality:** Fitch's review and analysis of the origination process determines whether Fitch decreases default rates by up to 25% or increases them by 0%-200%.



**Loss Severity**

To estimate loss severity on the mortgage loans in Spain, Fitch examined house price movements in Spain on a regional basis from 1987–2001. Fitch found significant differences in price development among the regions, mainly between the regions of Madrid, Catalonia, the Basque Country, and the rest of the regions in Spain. The cities of these regions have experienced higher price increases than other cities in Spain. As in most other countries, rural areas tend to develop on a more stable basis. Based on its analysis of the real estate market, Fitch assumed slightly higher market value declines for certain regions and for some large urban areas.

To derive market value declines for the respective stress scenarios, Fitch then compared the characteristics of the Spanish real estate market with markets in other European countries. As with its other European mortgage default models, Fitch has increased market value declines for higher value properties. These properties are generally subject to larger market value declines in a deteriorating market than homes with average or below-average market values due to limited demand for such properties.

When calculating recovery value, Fitch's model reduces each property value by the market value decline, external foreclosure expenses, and the cost to the servicer of carrying the loan from delinquency through default. For Spain, Fitch assumes external foreclosure costs represent 10% of the loan's balance at the time of default. Loss severity also incorporates the fact that the length of time of the foreclosure process might be longer than the actual one in a recession period. To calculate carrying costs, Fitch uses a worst-case scenario analysis, one that assumes the borrower does not pay any interest and the collateral is not realised for a period of three years.

**Excess Spread**

Excess spread represents the monetary difference between the income received by the issuer from the borrowers and the interest on the notes and other expenses paid by the issuer. Any reserve fund will be replenished from available excess spread, if it is drawn. The actual value of excess spread depends on levels of delinquencies, defaults, and prepayments, as well as the weighted average interest rate of the reference mortgage portfolio throughout the life of a transaction. The Threshold Rate calculation is designed to guarantee the issuer a minimum level of excess spread.

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