Valencia Hipotecario 3 Fondo de Titulización Activos

RMBS / Spain

This pre-sale report addresses the structure and characteristics of the proposed transaction based on the information provided to Moody's as of Octubre2006. Investors should be aware that certain issues concerning this transaction have yet to be finalised. Upon conclusive review of all documents and legal information as well as any subsequent changes in information, Moody's will endeavour to assign definitive ratings to this transaction. The ***definitive*** *ratings may differ from the* ***provisional*** *ratings set forth in this report. Moody's will disseminate the assignment of definitive ratings through its Client Service Desk. This report does not constitute an offer to sell or a solicitation of an offer to buy any securities, and it may not be used or circulated in connection with any such offer or solicitation.*

Estimated Closing Date

15 November 2006

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PROVISIONAL (P) RATINGS

Class	Rating	Amount (million)	% of Notes	Legal Final Maturity	Coupon
A1	(P)**Aaa**	€[90.0]	9.99	Sep. 44	3mE + [•]%
A2	(P)**Aaa**	€[780.7]	86.69	Sep. 44	3mE + [•]%
B	(P)**A2**	€[20.8]	2.31	Sep. 44	3mE + [•]%
C	(P)**Baa3**	€[9.1]	1.01	Sep. 44	3mE + [•]%
D	(P) **Ca**	€[10.4]	1.15	Sep. 44	3mE + [•]%
Total		€[911.0]			

The ratings address the expected loss posed to investors by the legal final maturity. Moody's ratings address only the credit risks associated with the transaction. Other non-credit risks have not been addressed, but may have a significant effect on yield to investors.

* *In Moody's opinion, the structure allows for timely payment of interest and ultimate payment of principal at par on or before the rated final legal maturity date on Series A1/A2/B/C, and for ultimate payment of interest and principal at par on or before the rated final legal maturity date on Class D.*

OPINION

Strengths of the Transaction

- Good quality collateral in terms of LTVs and seasoning (WALTV 63.70%)
- Good performance on the previous transaction
- Credit enhancement provided by a reserve fund and the subordination of the notes
- Reserve fund fully funded upfront available to cover potential shortfall in interest and in principal
- Basis swap provided by Banco de Valencia **(A2-P-1)**
- Excess spread-trapping mechanism through an 18 month "artificial write-off" mechanism
- 100% of the portfolio is paid via direct debit
- All loans to be transferred at closing date will be fully performing

Weaknesses and Mitigants

- Geographical concentration in the region of Valencia (67.72%), mitigated in part by the fact that this is Banco de Valencia's region of origin, where it has its highest expertise. Additionally, Moody's points out the potential increase in the volatility of losses due to the highest concentrations requiring additional credit enhancement.
- Pro-rata amortisation of the B and C Series of notes leads to reduced credit enhancement of the senior series in absolute terms. This is mitigated by strict triggers which terminate the pro rata amortisation of the notes as the performance of the transaction deteriorates.
- Lack of information (Employment); however a penalty was accordingly applied when calculating the credit enhancement.
- The deferral of interest payments on both classes B and C benefits the repayment of the series senior to each of them, but increases the expected loss on class B and C themselves. The reserve fund and the subordination have been sized accordingly to account for this deterioration on the expected loss.

STRUCTURE SUMMARY

Issuer:	Valencia Hipotecario 3 Fondo de Titulización de Activos (FTA)
Structure Type:	Senior / Mezzanine / Subordinated / Reserve fund
Seller/Originator:	Banco de Valencia (**A2**/**P-1**)
Servicer:	Banco de Valencia (**A2**/**P-1**)
Back-up Servicer:	N.A.
Interest Payments:	Quarterly on 22nd March, June, September and December – first payment date 22 March 2007
Principal Payments:	Pass-through on each payment date
Credit Enhancement/Reserves:	Excess spread per annum Reserve fund Subordination
Liquidity Facility:	N.A.
Hedging:	Basis swap to cover interest rate risk
Swap provider:	Banco de Valencia (**A2**/**P-1**)
Principal Paying Agent:	Bancaja (**A1**/**P-1**)
Management Company:	Europea de Titulización S.F.G.T.; S.A
Arranger/Lead Manager:	Bancaja, Banco de Valencia

COLLATERAL SUMMARY (PROVISIONAL POOL AS OF 23 OCTOBER 2006)

Loan Amount:	€984,552,228
Loans Count:	10,432
Pool Cut-off Date:	23 October 2006
WA Original LTV:	68.58%
WA Current LTV:	63.70%
WA Seasoning:	1.95 Years
WA Remaining Term:	21.99 Years
Interest Rate Type:	100% Floating
Geographic Diversity:	67.73% Valencia
Loan Purpose:	Primarily to acquire or refurbish a residence located in Spain
WA Loan Size:	€94,378

TRANSACTION SUMMARY

Third Securitisation by Banco de Valencia

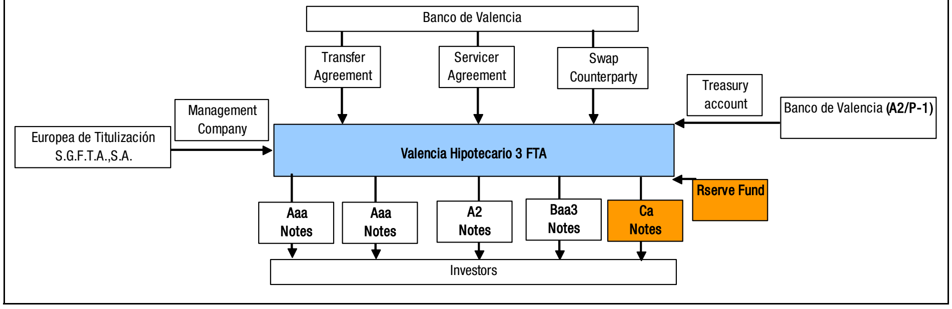
Valencia Hipotecario 3 Fondo de Titulización de Activos (hereafter referred to as the *"Fondo"*) is the third securitisation by Banco de Valencia.

The purpose of the transaction is to obtain liquidity and remove the credit risk linked to mortgages on Banco de Valencia's balance sheet. In this transaction, Banco de Valencia will sell a portfolio of mortgage loans to the *Fondo*, a special purpose vehicle (SPV). The *Fondo* will in turn issue five Series of notes to fund the purchase of the mortgage loan portfolio. The product being securitised consists of traditional first-lien mortgage loans.

Plain Vanilla Transaction

Chart 1:

Structure Diagram



STRUCTURAL AND LEGAL ASPECTS

Borrower payments swept into Banco de Valencia GIC account every week

Banco de Valencia will hold the Guaranteed Interest Contract (GIC) account. All of the payments under the loans in the mortgage portfolio are collected by the originator under a direct debit scheme and are paid directly into the GIC on a weekly basis. The amount in the GIC must be transferred by the originator to the paying agent (Bancaja **A1/P-1**) every payment date.

Moody's has set up some triggers in order to protect the GIC account from the possible loss of the treasury holder's **P-1** short-term rating. Therefore, if Banco de Valencia is downgraded below **P-1**, the management company will have the following options:

– To transfer the fund's treasury account to an institution whose rating is **P-1**

– To obtain a **P-1** rated entity to guarantee the fund's Security

Reserve fund fully funded at closing from the proceeds of the issue of the class D Notes

The reserve fund is designed to help the fund meet its payment obligations. It will be held at Banco de Valencia. The reserve fund will be used to protect the Series A1, A2 B and C notes against interest and principal shortfall on an ongoing basis. It may be amortised over the life of the transaction so that it amounts to the lesser of the following amounts:

1) 1.15% of the initial balance of the notes

2) The higher of the following amounts:

- 2.30% of the outstanding notional balance of the notes
- €5.2 million

However, amortisation of the reserve fund will cease if any of the following scenarios occur:

– The arrears level (defined as the percentage of non-written-off loans that are more than 90 days in arrears) exceeds 1.00%.

– The available amount under the reserve fund is not equal to the then required amount

– The weighted average interest rate under the loans is lower than 0.50%

In addition, the reserve fund will not amortise during the first 36 months of the life of the transaction

Basis Swap to cover interest rate risk

According to the swap agreement entered into between the Fondo and Banco de Valencia,

– The *Fondo* will pay the interest due from the non-written-off loans since the previous payment date less the amount of interest corresponding to the margin

– Banco de Valencia will pay the index reference rate on the notes over a notional calculated as the daily average of the outstanding amount of the non-written-off loans since the most recent payment date.

In the event of Banco de Valencia's long-term rating being downgraded below A2 or P-1, it will have 10 days within which to (i) collateralise its obligation under the swap for an amount sufficient to maintain the then current rating of the notes; or (ii) find a suitably rated guarantor or substitute.

Payment Structure Allocation

On each quarterly payment date, the *Fondo's* available funds (principal received from the asset pool, the Reserve Fund, amounts received under the swap agreement and interest earned on the transaction accounts) will be applied in the following simplified order of priority:

1) Cost and fees, excluding servicing fee
2) Any amount due under the swap agreement (except termination payments if Banco de Valencia defaults under the swap agreement)
3) Interest payment to Series A1 and A2 notes
4) Interest payment to Series B notes (if not deferred)
5) Interest payment to Series C notes (if not deferred)
6) Retention of an amount equal to the principal due under the notes
7) Interest payment to Series B notes (if deferred)
8) Interest payment to Series C notes (if deferred)
9) Replenishment of the reserve fund
10) Interest payment to Series D notes
11) Principal payment to series D notes
12) Termination payments under the swap agreement upon default of Banco de Valencia
13) Junior expenses

Interest Deferral Mechanism

The payment of interest on the Series B and C notes will be brought to a more junior position if, on two consecutive payments dates, the following criteria are met:

Table 1:

Series B		Series C	
a)	The principal deficiency exceeds 50% of the outstanding balance of Series B plus 100% of the outstanding balance of Series C	a)	The principal deficiency exceeds 50% of the outstanding balance of Series C
b)	Series A1and A2 are not fully redeemed	b)	Series A1, A2 and Series B are not fully redeemed

18-month "artificial write-off" mechanism

The transaction structure for classes A, B, and C benefits from an "artificial write-off", which traps available excess spread to cover losses (if any). This type of "artificial write-off" is hidden in the definition of Principal Due, which is the difference between the A1,A2 B, and C notes outstanding and the outstanding performing loans (loans less than 18 months in arrears).

Class A Amortisation

Until the payment date on which the Series B, and C notes will start to amortise pro-rata with Class A, the amount retained as principal due will be used for the repayment of Class A in the following order of priority:

1) Amortisation of Series A1 notes
2) The Series A2 notes will start to amortise once the Series A1 notes have been fully amortised,

Nevertheless, the amount retained as principal due will be distributed pro-rata among Series A1 and A2, if the amount of loans more than 3 months and less than 18 months in arrears exceeds [1.50%] of the outstanding balance of the portfolio

Pro rata amortisation

This transaction also includes pro rata amortisation. This amortisation entails risk, as opposed to fully sequential transactions, given that the credit enhancement decreases in absolute terms. The risks introduced by pro-rata amortisation are mitigated by the following triggers:

– Series B Notes will start amortising pro rata with the Class A notes when they represent 4.61% of the outstanding balance under the Series A1, A2, B and C notes
– Series C Notes will start amortising pro rata with the Class A and B notes when they represent 2.02% of the outstanding balance under Series A1, A2, B and C notes

However, the pro rata amortisation will cease if:

Table 2:

Class B	**Class C**
The loans more than 90 days in arrears and less than 18 months exceed 1.00%	The loans more than 90 days in arrears and less than 18 months exceed 0.75%
The cash reserve is not funded at the required level	
The loan balance is less than 10% of the initial loan balance	

Class D amortisation

The Series D notes will amortise, on each payment date, for an amount equal to the difference between the outstanding amount of the Series D notes and the reserve fund's required amount on the current payment date.

COLLATERAL

Good quality collateral in terms of LTV and seasoning

As of October 2006, the portfolio comprised 10,432 loans, representing a provisional portfolio of €984,552,228. The loans have been contracted to individuals located in Spain. The loans consist of first-lien mortgages on residential properties. All the properties on which the mortgage security has been granted are covered by property damage and fire insurance. At closing date there are no loans in arrears. The average loan is €94,378 and the largest borrower is €948,593.

Chart 2:
Portfolio Breakdown by Geographical Diversification

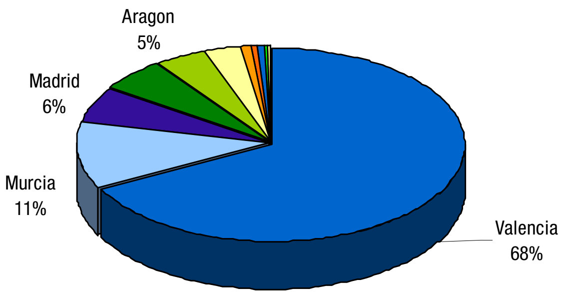
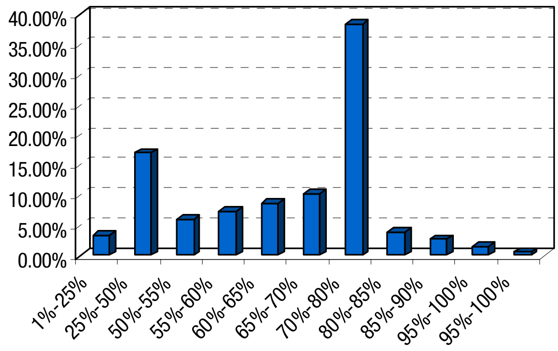


Chart 3:
Portfolio Breakdown by LTVs



The loans were originated between 1996 and 2006, with a weighted average seasoning of 1.95 years and a weighted average remaining maturity of 21.99 Years. Almost all the loans paid via monthly instalments, which are debited to accounts held by the debtors at Banco de Valencia. Moody's views this feature as a positive characteristic since delinquencies are likely to be tracked more easily.

Chart 4:
Portfolio Breakdown by Occupancy Type

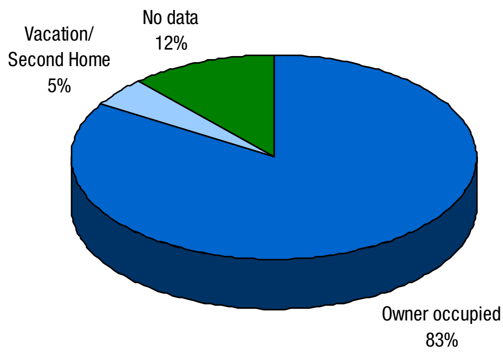
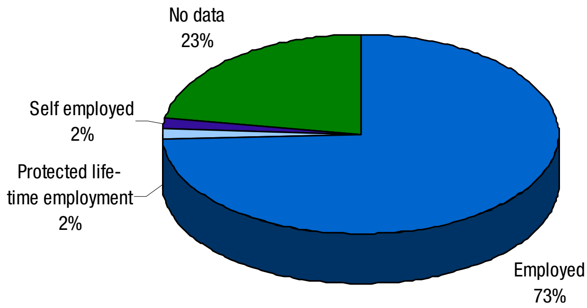


Chart 5:
Portfolio breakdown by Employment Type



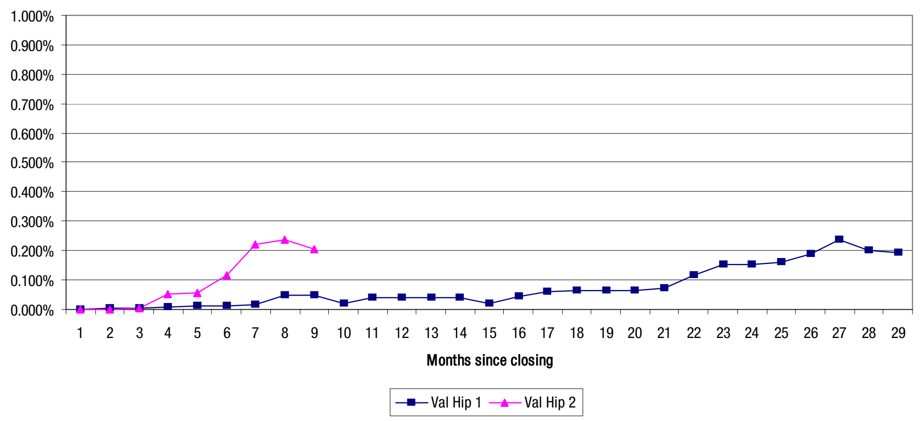
Renegotiations

Any renegotiation of the terms and conditions of the loans is subject to the *gestora*'s (lender's) approval. The *gestora* may authorise the originators to renegotiate the interest rate or the maturity of the loans subject to the following conditions:

- If the weighted average margin of the loans is less than 0.60%, the originator has agreed to pay the fund the modified margin, for each revised participated loan, until the loan is repaid. However, no additional renegotiations are allowed once the weighted average margin on the loans falls below 0.50%.
- The global initial amount of loans on which the maturity has been extended cannot be greater than 10% of the initial amount of the pool. In any case, the extension of any loan's maturity profile must comply with the following standards:
  - The maturity of any loan cannot be postponed later than April 2041.
  - The frequency of payments cannot be decreased.
  - The repayment system cannot be modified.

Performance Data on Previous Valencia Hipotecario transactions

Chart 6:
Delinquencies 90 +



ORIGINATOR, SERVICER AND OPERATIONS REVIEW

Banco de Valencia was recently rated (A2/P-1)

Banco de Valencia (rated **A2**/**P-1**/**C**), with total assets of around €12 billion and 388 branches as at December 2005, is a medium-sized Spanish retail and commercial bank with a good business franchise in the prosperous south-eastern region of Valencia.

Banco de Valencia is the third-largest player in the Valencia region, with market shares as at September 2005 of 30.4% for deposits and 14.5% for loans, behind Caja de Ahorros de Valencia, Castellón y Alicante (Bancaja, rated **A1**/**P-1**/**B-**), the market leader and the parent company of Banco de Valencia, and Caja de Ahorros del Mediterráneo (**A1**/**P-1**/**B-**). Valencia is a key economic region in Spain, accounting for around 10% of the population and 10% of domestic GDP. The economy is relatively diversified and includes industries such as automotive manufacturing, chemicals, textiles, furniture, ceramics, toy manufacturing and, above all, tourism.

Spurred by strong competition and diminishing margins, the bank has diversified its geographical presence to other parts of Spain over recent years, particularly along the east cost. In addition to over 300 branches in the Valencia region, the bank now has 27 branches in Madrid, 18 in Almería, 15 in Barcelona, and 17 in various other towns and cities.

Banco de Valencia is 38.4% owned by Bancaja, the sixth-largest financial institution and the third-largest savings bank in Spain by assets, as well as the market leader in the Valencia region with market shares of around 30% for deposits and 20% for loans. Although Banco de Valencia is not majority owned by Bancaja, it is fully consolidated in Bancaja's accounts. As of December 2005, Banco de Valencia had total assets of €12 billion and net profit of €95.7 million for the year, representing around 20% of Bancaja's consolidated total assets and 29% of its net profit.

MOODY'S ANALYSIS

Determination of lognormal loss distribution.

The first step in the analysis is to determine a loss distribution for the pool of mortgages to be securitised. Due to the high volume of loans and supporting historical data, Moody's uses a continuous distribution model to approximate the loss distribution: lognormal distribution.

In order to determine the shape of the curve, two parameters are needed: the expected loss and the volatility associated with this expected loss. These parameters are derived from the Moody's Individual Loan Analysis ("MILAN") model.

In order to extrapolate expected losses for the loan pool, Moody's has compared the underwriting criteria of the originators with those of other mortgage originators in Spain.

Moody's thus determines a number representing the enhancement that would be required for a pool of mortgages to obtain a 'Aaa' rating under highly stressed conditions. This credit enhancement number (the "Aaa CE" number) is obtained by means of a loan-by-loan model.

The "Aaa CE" number is determined by using "MILAN", Moody's loan-by-loan model for rating RMBS transactions

The "MILAN" model looks at each loan in the pool individually and, based on its individual characteristics such as LTV or other identified drivers of risk, computes a benchmark CE number. This number assumes stressed recovery rates (through house price decline), interest rates and costs of foreclosure, as well as a stressed recovery time. The weighted average benchmark CE number is then adjusted according to the positive and negative characteristics of each loan and to those of the pool as a whole, in order to produce the "Aaa CE" number.

The "Aaa CE" number and the Expected Loss Number form the basis of Rating Committee discussions and are used to derive the lognormal distribution of the pool losses.

The standard deviation of the distribution is found by setting the probability of a loss greater than the expected loss that is consistent with the Idealised Expected Loss target of the "Aaa CE" number.

"MARCO", Moody's cash-flow model, is used to assess the impact of the structural features of RMBS transactions

Once the loss distribution of the pool under consideration has been computed, a cash flow model, Moody's Analyser of Residential Cash-Flows ("MARCO"), is used to assess the impact of structural features of the transaction, such as the priorities of interest and principal, and the related triggers, swap features and excess margins, liquidity mechanisms and the value of excess spread.

The sum of the loss experienced per note Class in each scenario, weighted by the probability of such loss scenarios, will then determine the expected loss on each tranche and hence the rating, in line with Moody's target losses for each rating category.

RATING SENSITIVITIES AND MONITORING

In its capacity as management company, Europea de Titulización S.G.F.T, S.A will prepare quarterly monitoring reports with respect to the portfolio and payments to the notes. These reports will detail the amounts received by the issuer during each collection period and will provide portfolio data. Moody's will monitor this transaction on an ongoing basis to ensure that it continues to perform in the manner expected, including checking all supporting ratings and reviewing periodic servicing reports. Any subsequent changes to the rating will be publicly announced and disseminated through Moody's Client Service Desk. For updated monitoring information, please contact monitor.madrid@moodys.com

RELATED RESEARCH

For a more detailed explanation of Moody's rating approach to this type of transaction, similar transactions and performance data, please refer to the following reports:

Special Reports

- Introducing Moody's Arrears Index for Spanish Mortgage-Backed Securities, March 2002 (SF12700)
- Moody's Spanish RMBS Arrears Index: Delinquency Levels Remained Persistently Low in 2002 But Are Likely To Rise Given Weakening Global Economy And Factors Affecting Homeowners' Indebtedness, May 2003 (SF21607)
- Structural Features in the Spanish RMBS Market Artificial Write-Off Mechanisms: Trapping the Spread, January 2004 (SF29881)

Performance Review

- Spanish RMBS Q3 2004 Performance Review, February 2005 (SF50365)

Rating Methodologies

- Moody's Approach to Rating Spanish RMBS: The "MILAN" model, March 2005 (SF49068)

Pre-Sale Reports

- Valencia Hipotecario 1, April 2004 (SF35214)
- Valencia Hipotecario 2, November 2005 (SF65627)

Performance Overviews

- Valencia Hipotecario 1
- Valencia Hipotecario 2

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients

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