Valencia Hipotecario 5, FTA

New Issue

Inside This Report

Related New Issue Appendix

Valencia Hipotecario 5, FTA

Related Research

Representations, Warranties, and Enforcement Mechanisms in Global Structured Finance Transactions

Analysts

Covadonga Aybar
+34 91 702 5775
covadonga.aybar@fitchratings.com

Carlos Masip
+34 91 702 5773
carlos.masip@fitchratings.com

Mirella Tinti
+44 20 3530 12 41
mirella.tinti@fitchratings.com

Capital Structure

Class	Amount (EUR)	Final Maturity	Rating	CE (%)[a]	Outlook	TT[b] (%)	TTLM[c]
A	379.3	February 2047	Asf	13.83	Stable	92.22	19.4
B	5	February 2047	NR	12.61	NR	1.22	0.3
C	27	February 2047	NR	6.05	NR	6.56	1.4
Total Issuance	**411.3**						

Closing occurred on 16 December 2008. The transfer of the portfolio to the issuer occurred on 22 December 2008. The ratings assigned above are based on the portfolio information as of 16 January 2012, provided by the originator
[a] Structural credit enhancement (CE) on the class A notes comprises the subordination of class B (1.22%) and C (6.56%) and a cash reserve fund (6.05%)
[b] Tranche Thickness (TT) percentage – ratio of class size to collateral balance
[c] Tranche Thickness Loss Multiple – TT% divided by Fitch's base case loss expectation. See also *Structured Finance Tranche Thickness Metrics*, dated 29 July 2011

Transaction Summary%

This transaction is a cash flow securitisation of a EUR500m static pool of Spanish residential mortgage loans issued by Valencia Hipotecario 5, FTA (the issuer). It originally closed in December 2008, with a pool factor of 0.82 as of November 2011. The loans have been originated and serviced by Banco de Valencia (the seller and the servicer, 'BB−'/Stable/'B').

Fitch Ratings assigned a rating to the class A notes, as listed above, in February 2012. The rating addresses the payment of interest on the notes according to the terms and conditions of the documentation, and the repayment of principal by the notes' legal final maturity date.

Key Rating Drivers

Non-Prime Collateral: The agency has identified the presence of diverse risk attributes, such as loans with high original loan-to-value ratios (OLTV), which account for 21.04% of the pool. Additionally, 16.63% of the collateral has been originated through non-traditional branch network channels and 13.97% of the loans were granted to non-Spanish borrowers. The risk attributes of the collateral have been captured in line with Fitch's RMBS criteria Spanish Addendum and are reflected in the assigned rating.

Weak Performance Since Closing: Fitch has observed volatility in the volume of reported arrears in between payment periods, as mid-monthly pool cuts show higher arrears levels than month-end cuts. This is mainly explained by Banco de Valencia's recovery procedures and the borrowers' behaviour.

This volatility brings additional credit risk to the transaction and Fitch has consequently incorporated borrower performance history into its analysis. Moreover, Fitch has applied its foreclosure frequency (FF) matrix to the pool, provided as of mid-month January 2012, in order to capture these riskier borrowers.

Reserve Fund Increased: Upon the assignment of ratings by Fitch in February 2012, the reserve fund was increased to EUR24.88m from the initial EUR18.5m and the transaction documents were amended to reflect Fitch's applicable criteria.

Servicer Disruption Risk Mitigated:. Fitch has analysed the payment interruption risk the transaction could suffer in case of servicing disruptions. Fitch believes the risk is sufficiently mitigated, considering Banco de Valencia has funded a cash deposit in the name of the issuer which covers for senior costs, net payment of the swap, and six months interest due amounts on the class A notes. Moreover, the servicer is transferring loan cash collections on a daily basis to the issuer's treasury account, held at Banco Santander ('A'/Negative/'F1').

Key Parties

- **Originator, Seller and Servicer of the Collateral:** Banco de Valencia 'BB-'/Stable/'B'
- **Account Bank:** Banco Santander 'A'/ Negative/'F1'
- **Paying Agent:** Banco Cooperativo Español 'BBB+'/Negative/'F2'
- **Swap Provider:** JP Morgan Securities Ltd (not rated) linked to JP Morgan Chase NA 'AA-'/Stable/'F1+'
- **Issuer:** Valencia Hipotecario 5, FTA
- **Management Company:** Europea de Titulización S.A., S.G.F.T.

Related Criteria

EMEA RMBS Master Rating Criteria (August 2011)
EMEA Residential Mortgage Loss Criteria (August 2011)
EMEA Criteria Addendum - Spain (August 2011)
EMEA RMBS Cash Flow Analysis Criteria (June 2011)
Counterparty Criteria for Structured Finance Transactions (March 2011)
Counterparty Criteria for Structured Finance Transactions: Derivative Addendum (March 2011)
EMEA RMBS Legal Assumptions (June 2011)

Rating Sensitivity[1]

This section of the report provides a greater insight into the model-implied sensitivities the transaction faces when one risk factor is stressed, while holding others equal. The modelling process first uses the estimation and stress of base case assumptions to reflect asset performance in a stressed environment, and secondly, the structural protection is analysed in a customised proprietary cash flow model (see section *Financial Structure & Cash Flow Modelling*). The results below should only be considered as one potential outcome given that the transaction is exposed to multiple risk factors that are all dynamic variables.

Rating Sensitivity to Defaults

The table below reflect changes if the base case default rate for the portfolio is increased by a relative amount. For example, increasing the base case default rate by 25% may result in a two-notch downgrade of the class A from 'Asf' to 'BBBsf'.

Rating Sensitivity to Default Rates

	Class A
Original rating	Asf
10% increase in default rates	A-sf
15% increase in default rates	BBB+sf
25% increase in default rates	BBBsf

Source: Fitch

Rating Sensitivity to Recovery Rates

The change in rating if the base case recovery rates are adjusted is demonstrated below. Rating sensitivity to recovery rates is lower than to variations in the default rates. Haircutting the assumed recovery rates by 10%, 15% and 25% results in a one-notch and two-notch model-implied downgrade of the class A notes.

Rating Sensitivity to Recovery Rates

	Class A
Original rating	Asf
10% decrease in recovery rates	A-sf
15% decrease in recovery rates	A-sf
25% decrease in recovery rates	BBB+sf

Source: Fitch

Rating Sensitivity to Shifts in Multiple Factors

The table below summarises the rating sensitivity to a multiple factor stress (both weighted average foreclosure frequency (WAFF) and weighted average recovery rate (WARR) simultaneously). The model-implied results show that the senior class would suffer downgrades of two or three notches in scenario 1 to 2. The agency also tested a third scenario by applying a combination of increasing defaults and reducing recoveries by 25%; such stress would cause the class A to suffer a four-notch downgrade from 'Asf' to 'BBB-sf'.

Rating Sensitivity to Default Rates and Recovery Rates

	Class A
Original rating	Asf
Scenario 1: 10% increase in default rates, 10% decrease in recovery rates	BBB+sf
Scenario 2: 15% increase in default rates, 15% decrease in recovery rates	BBBsf
Scenario 3: 25% increase in default rates, 25% decrease in recovery rates	BBB-sf

Source: Fitch

[1] These sensitivities only describe the model-implied impact of a change in one of the input variables. This is designed to provide information about the sensitivity of the rating to model assumptions. It should not be used as an indicator of possible future performance

Model, Criteria Application and Data Adequacy

Fitch was given dynamic delinquencies (based on loans more than 90 days in arrears) for the overall residential mortgage loan portfolio of the seller, as well as static historical data for the Valencia Hipotecario series including delinquencies, recoveries, cumulative defaults and prepayments. The seller also provided information on repossessed real estate assets. The agency received loan-by-loan information for nearly all the fields it requires under its updated RMBS data requirements. For missing or incomplete fields, Fitch has applied conservative assumptions.

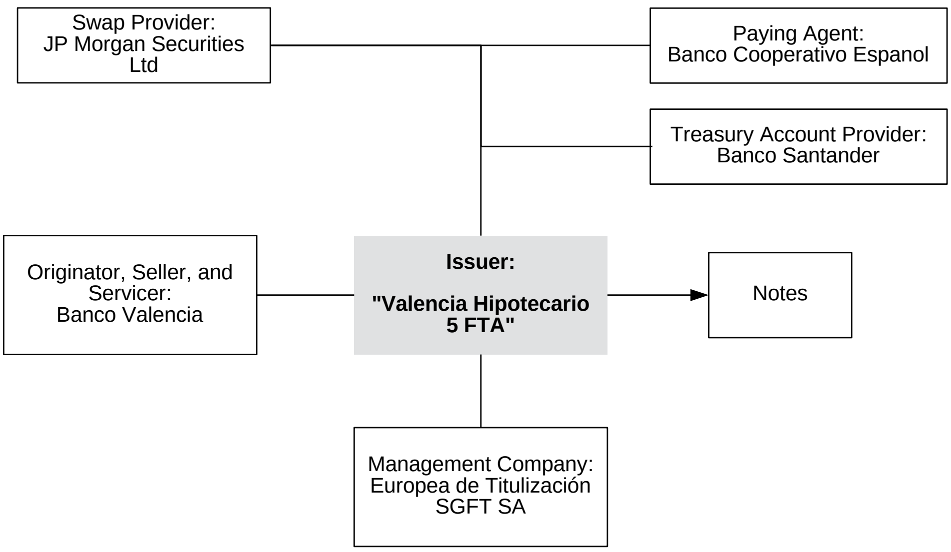
Fitch has analysed the obligor default risk using its proprietary Spanish RMBS default model (see *EMEA Residential Mortgage Loss Criteria and EMEA Criteria Addendum – Spain,* dated August 2011). The agency's proprietary cash flow model has been used to complete the rating analysis and simulate the transaction cash flows and capital structure. Fitch's cash flow model has been customised to account for the specific features of the deal.

Fitch reviewed the audit report regarding the data provided by SPV management company (Europea de Titulización S.A., S.G.F.T. or the Gestora). An internationally recognised audit firm conducted the report, which included a detailed review of 461 loans from 4.380 loan files. Fitch believes the sample size, the scope of the audit report and the lack of material error findings suggest the originator provided an acceptable quality of data. In addition, Fitch conducted its own file review consisting of ten loans and the agency discovered no material errors. As a result, Fitch made no adjustments to its analysis with respect to the data provided.

Transaction and Legal Structure

Figure 1

Structure Diagram



Source: Transaction documents

Legal Framework

The issuer is Valencia Hipotecario 5, FTA, a limited-liability SPV incorporated under the laws of Spain, the sole purpose of which is to acquire the mortgage loans from Banco de Valencia as collateral for the issuance of quarterly-paying notes. However, under Spanish law, mortgage loans are not actually transferred, as this would entail a lengthy process of re-registering the mortgages at the property registry. Instead, mortgage originators are permitted to issue mortgage certificates (Certificados de Transmisión Hipotecaria or CTH).

At closing, the CTHs were acquired from the seller on behalf of the fund by Europea de Titulización S.A., S.G.F.T., a limited liability company incorporated under Spanish laws, the activities of which are limited to the management of securitisation funds.

The gestora, which is supervised by the Comisión Nacional del Mercado de Valores (CNMV), is responsible for cash reconciliation, payment and waterfall calculations and their reporting, including the monitoring of applicable triggers. It will also be responsible for taking any action in the interests of the noteholders, such as the replacement of the servicer, account bank or swap counterparty.

Representations and Warranties

The seller provided the issuer with specific representations and warranties (R&Ws) concerning the characteristics of the performing mortgages, and the general and legal circumstances of the loans in the portfolio. For more details, see the related *Appendix* which includes all the R&Ws given by the transaction parties. The R&Ws are substantially comparable to those typically contained in Spanish RMBS transactions, as described in Fitch's research *Representations, Warranties, and Enforcement Mechanisms in Global Structured Finance Transactions*, dated 23 December 2011. Hence, Fitch made no adjustments to its analysis with respect to the R&Ws.

Substitution of the Assets

Like most Spanish RMBS transactions, only those loans that do not comply with the representations and warranties will be allowed to be substituted. Such substitution must follow the rules laid out in the transaction documentation and Spanish Securitisation Law.

Loans that have breached the R&W will either be fully amortised or substituted by the seller with a mortgage similar in amount and characteristics. The substitution will have to be approved by the management company. The substitution cost will be paid by the originator.

Permitted Variations on the Assets

The seller, in administering the mortgage loans, should not without the consent of the management company, voluntarily cancel the mortgages forming the collateral for reasons other than the full amortisation of the loan. Additionally, it will not renounce the mortgage loans, modify or restructure them, cancel them in whole or in part, or in general take any action that diminishes the rank of the loans, the legal effectiveness, or the economic value of the mortgage loans, except for the modifications listed below.

- To subrogate a mortgage loan only in cases where the characteristics of the new debtor are similar to those of the original one and in line with the originator's underwriting guidelines.
- To apply margin reductions, limited to the WA margin of the collateral that will not fall below 50bp. As no material margin compression has been observed since closing, Fitch did not apply any adjustment when modelling the transaction.
- To modify the term to maturity of a mortgage loan as long as the amortisation method is maintained and the frequency of instalments remains unchanged or is increased. Any extension is limited to the final maturity of the longest loan (5 July 2043). The outstanding amount of the mortgage loans on which the extension of maturity could be allowed will not exceed 10% of the initial pool balance.

Historically, limited loan modifications or restructurings have been reported for existing RMBS transactions. However, given the downturn in the housing market and macroeconomic conditions, many lenders have expanded their loan modification and restructuring programmes as part of loss mitigation strategies. Fitch expects that all loan modifications or restructurings will be conducted within the above limits.

Fitch has analysed loan-by-loan modification data of Valencia Hipotecario RMBS transactions and the reported data suggests low materiality. Figure 2 summarises the volume of loan modifications of Valencia Hipotecario deals rated by Fitch, as of December 2011.

Figure 2

Loan Modifications

RMBS transactions rated by Fitch	Closing date	Number of loans at closing	Number of modified loans	Loan modifications/ original pool ratio (%)
Valencia Hipotecario 1, FTA	23 Apr 2004	8,531	248	2.9
Valencia Hipotecario 2, FTH	07 Dec 2005	12,241	342	2.8
Valencia Hipotecario 3, FTA	15 Nov 2006	9,544	238	2.5
Valencia Hipotecario 4, FTA	21 Dec 2007	6,925	186	2.7

Source: Fitch, based on Gestora data reported as of December 2011

Disclaimer

For the avoidance of doubt, Fitch relies, in its credit analysis, on legal and/or tax opinions provided by transaction counsel. As Fitch has always made clear, Fitch does not provide legal and/or tax advice or confirm that the legal and/or tax opinions or any other transaction documents or any transaction structures are sufficient for any purpose. The disclaimer at the foot of this report makes it clear that this report does not constitute legal, tax and/or structuring advice from Fitch, and should not be used or interpreted as legal, tax and/or structuring advice from Fitch. Should readers of this report need legal, tax and/or structuring advice, they are urged to contact relevant advisers in the relevant jurisdictions.

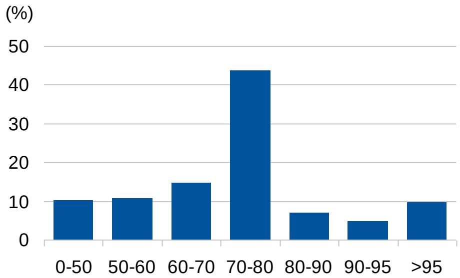
Asset Analysis

As of 16 January 2012, the portfolio had an outstanding balance of EUR407m, comprising 3,373 residential mortgage loans backed by properties in Spain. The aggregate portfolio had a WA original loan-to-value (OLTV) of 72.8%. Fitch has identified loans with high LTV; 21.04% of the mortgage loans had LTVs above 80%. This is a well seasoning pool (52 months) and the most representative vintages of origination are 2007 and 2008, representing 47.2% and 39.7% respectively.

Figure 3

Valencia Hipotecario 5 FTA

OLTV distribution by current balance

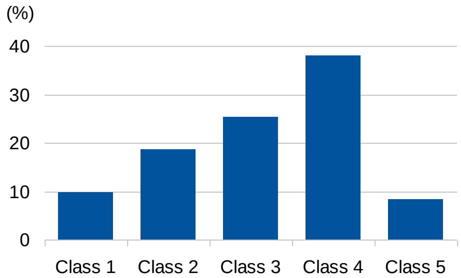


Source: Pool cut (January 2012)

Figure 4

Valencia Hipotecario 5 FTA

Fitch DTI distribution by current balance

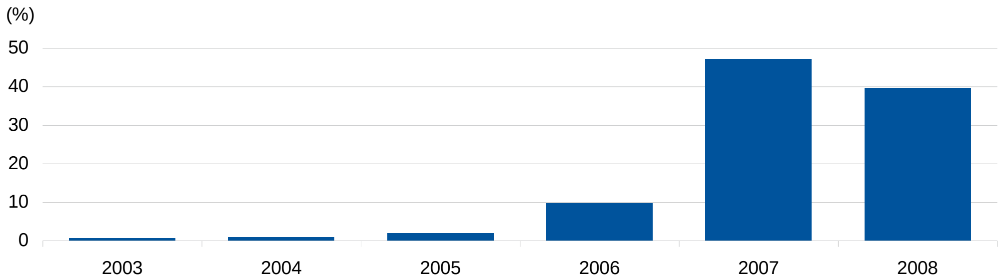


Source: Pool cut (January 2012)

Figure 5

Valencia Hipotecario 5 FTA

Portfolio distribution per year of origination



Source: Pool cut (January 2012)

Lender Adjustment

Fitch's base default probabilities assume that origination, underwriting and servicing practices and procedures are in line with those of a standard Spanish lender with market expertise. As part of its analysis, the agency performs an operational review of the originator to assess the origination, underwriting and servicing capabilities of the seller. The agency also considers certain elements not factored into the loan-by-loan analysis, either because they are not available or because they are only applicable on an aggregate basis, such as: (i) historical performance of the mortgage loans originated by the lenders; (ii) length of historical performance observation period; (iii) performance of previously securitised deals; and (iv) undisclosed information.

When comparing historical information provided for the issuer's portfolio with the WA frequency of foreclosure (FF) resulting from the loan-by-loan analysis, Fitch concluded that no further adjustment was needed. This indicates that the risk attributes of the portfolio have already been captured by the overall probability-of-default matrix and the adjustments made in light of the loan and borrower characteristics.

Affordability

Fitch was provided with loan-by-loan DTI information for 100% of the pool, as shown in Figure 6. However, the originator did not provide monthly income data for the securitised pool. In order to calculate Fitch's conservative DTI, the agency derived the annual net income based on the calculated annual instalments, taking into account interest rates at origination, original loan amount and original term to maturity.

Figure 6

DTI Class Distribution According to Fitch Calculations

DTI class/% of the pool	Fitch calculation	Data provided
Class 1	9.75	10.24
Class 2	18.65	19.56
Class 3	25.31	26.00
Class 4	38.03	38.88
Class 5	8.26	5.32

Source: Fitch

Borrower Profile

The seller provided employment data on a loan-by-loan basis for 91.2% of the loans in the portfolio. As of loan origination, 77.48% of the borrowers are employees of a third party, 10.54% are self-employed, 2.49% are civil servants and 0.72% are classified as unemployed.

Banco Valencia was not able to specify on a loan-by-loan basis the type of contract of the borrowers employed by a third party. However, Banco de Valencia has recently included more extensive employment information in its internal IT tools and has provided a breakdown of residential mortgage loans granted to individuals since 2008. Consequently, Fitch's has assumed that 6.39% of the borrowers in the pool had a temporary contract at origination, while 71.09% had a fixed one.

For self-employed, temporary, unemployed or none disclosed information, the base FF was increased by 25%.

Nationality

13.97% of the loans in the pool were granted to non-Spanish borrowers. Given the weak links of the immigrant population and their weaker historical performance, a 100% incremental FF hit was applied to those loans. The percentage of non-Spanish borrowers in this transaction is above the average for the Spanish market.

More Than Two Borrowers

4.32% of the loans in the pool were granted to more than two borrowers. As the need to include more than two borrowers for the same loan may indicate a weaker payment capacity of each borrower individually, the agency applied a 20% incremental FF hit to those loans.

Loan Purpose

96.61% of the loans were granted to purchase a house and 3.39% for home improvement. A 25% incremental FF has been applied to those loans other than for home acquisition.

Property Type

The pool comprises first-lean loans granted to individuals backed by mortgages on first (90.69%) and second (9.31%) properties in Spain. A financially stressed borrower is more likely to permit a default on a second home than on a primary residence; consequently, the FF for second homes has been increased in 25%.

Fitch addressed the recovery risk of residential mortgages using its RMBS market value decline (MVD) assumptions, which assign to each property the MVD corresponding to the region where it is located. The portfolio contains 2.42% of properties whose values are above or below the market average for their respective regions; therefore, a jumbo haircut has been applied in accordance with Fitch's criteria.

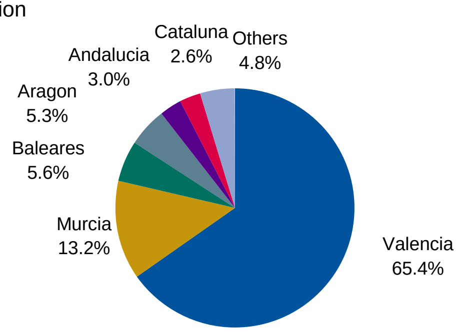
Geographical Concentration

The pool is significantly concentrated in Valencia, in line with Banco de Valencia's home market. 65.40% of the portfolio's outstanding balance is concentrated in the Valencia autonomous community. A geographical adjustment hit was applied by increasing the FF of those loans by 15%.

Figure 7

Valencia Hipotecario 5 FTA

Geographical distribution



Source: Pool cut (January 2012)

Origination Channel

Fitch received a loan-by-loan breakdown of the origination channel. According to this, 16.63% of the outstanding pool balance was originated through brokers, for which Fitch has increased the FF by 100%. According to the agency's analysis, non-traditional channels have a significantly greater impact on delinquencies than traditional branch subscriptions.

Performance Since Closing

There has been a moderate build-up of arrears since closing, while 2.62% of the original pool has been written off (defined as loans in arrears by more than 18 months). Fitch observed volatility in the volume of the arrears between payment periods. The level of loans in arrears in the three-months bucket has experienced a mid-monthly increase, that reduces again by the end of the month. The servicer affirmed that such movement is due to Banco de Valencia's recovery procedures and borrower behaviour. Borrowers under pressure pay one instalment, avoiding the beginning of the judicial process and going back to the two- to three-month bucket.

Fitch believes this credit behaviour is associated with weaker borrowers.

As of 31 December 2011, the level of arrears in the three-months buckets represented 3.01% of the current balance; however, as of 16 January 2012, this ratio stood at 5.60%. Fitch applied its FF matrix to the pool provided as of mid-month January to capture the mentioned volatility within its credit analysis.

Default Model Output

Figure 8 illustrates the asset analysis results across different rating scenarios. Fitch has used these WAFF and WARR levels when modelling the transaction cash flows.

Figure 8

Fitch Default Model Output

Rating level (%)	WAFF[a]	WARR[b]	MVD[c]
Asf	23.56	47.97	53.51
Bsf	11.97	60.35	43.34

[a] Weighted-average foreclosure frequency
[b] Weighted-average recovery rate
[c] Market value decline
Source: Fitch

Financial Structure and Cash Flow Modelling

Credit Enhancement

Subordination: At January 2012, structural credit enhancement (CE) for the class A notes, equivalent to 13.83%, was provided by the subordination of classes B (1.22%) and C (6.56%), plus a cash reserve fund (RF) of 6.05%.

Reserve Fund (RF): Upon the assignment of ratings by Fitch in January 2012, the RF was increased to EUR24.88m from the initial EUR18.5m; it is currently at EUR7.9m. The RF will be permitted to reduce to the lower of: i) EUR24.8m; and ii) the higher of: a) 12.10% of the outstanding class A, B and C notes' balance; and b) EUR12.44m.

This amortisation is subject to the following conditions: more than three years have passed since the closing date of the transaction, which is the case at present; arrears over 90 days lower than 1% over outstanding balance of the assets, excluding defaults; the WA margin of the collateral higher than 50bp; and the RF was at its target level on the previous payment date. As the 90 day+ trigger is breached (3.01% as of December 2012) the RF is not permitted to amortise at present.

Excess Spread: Mainly generated from the difference between the WA margin of the collateral (0.84%) and that of the notes (0.34%). The excess spread available in this transaction is tight, but provides the first layer of protection against credit losses.

Provisioning

The transaction benefits from a provisioning mechanism whereby defaulted loans, defined as loans more than 18 months in arrears, will be recorded as a loss and will form part of the principal redemption due amount.

Interest Rate Swap

At closing, the issuer entered into two swap agreements to mitigate basis and reset risk, one for the loans whose interest is revised annually and another for those loans where the rate is revised semi-annually. Under the terms of the swap, the issuer will pay the twelve-month Euribor received from the mortgages in exchange for the three-month Euribor payable on the notes, plus a guaranteed margin of 12bp on a notional defined as the balance of non-defaulted loans.

Priority of Payments

The transaction uses a combined waterfall of payments for principal and interest collections. In each quarterly payment date, amounts will be distributed according to the following order of priority.

Figure 9
Priority of Payments

1	Taxes and senior expenses
2	Net swap payment
3	Interest payments on the class A notes
4	Interest payments on the class B notes unless deferred
5	Interest payments on the class C notes unless deferred
6	Principal due on the class A, B and C notes
7	Interest on the class B notes if deferred
8	Interest on the class C notes if deferred
9	Replenishment of the reserve fund to its required level
10	Swap termination amounts and other subordinated amounts

Source: Transaction documents, Fitch

The interest on the class B and C notes will be deferred to a junior position in the waterfall if the cumulative defaults exceed 16% and 14% of the original collateral amount for the class B and C respectively. Defaults are defined as loans in arrears over 18 months. As cumulative defaults stand at 2.62% as of January 2012, the class B and C interest is not deferred.

Notes' Amortisation

Principal redemption on the notes is allocated sequentially, beginning with the class A notes and only moving through the subordinated classes once they have been redeemed in full. Once the class A notes have been fully redeemed, class B will start to amortise until its full redemption, followed by class C.

Nevertheless, if the following conditions are met, the class B and C notes can amortise pro rata with the class A notes:

- the RF is at its target level;
- more than 10% of the pool is still outstanding;
- the relative size of the respective series has doubled since closing in relation to the outstanding amounts of class C, B, and A notes; and
- the balance of loans more than 90 days in arrears is less than 1.5% and 0.75% of the outstanding balance of the collateral for the class B and C respectively (excluding written-off loans).

The final maturity date for the issuer is February 2047, three and a half years after the final scheduled maturity date for all loans in the collateral pool. Fitch considers this delay adequate to ensure that collections from the mortgages will be sufficient to redeem the obligations of the fund for any defaulted loans.

All notes are subject to a clean-up call option in favour of the management company when less than 10% of the initial collateral balance remains outstanding.

Scenario Testing

Fitch has tested the structure under the default distributions described in its *EMEA RMBS Cash Flow Analysis Criteria* (see *Related Criteria*). Different default vectors have been tested combined with different prepayments (high/low) and interest-rate environments (rising/stable/decreasing). Assumptions used under individual scenarios were in accordance with Fitch's cash flow analysis criteria for RMBS.

Fitch modelled the cash flows from the mortgages based on the WARR and WAFF provided by the loan-by-loan collateral analysis. The cash flow model assumes that defaults are spread over the first seven years and considers the cost of carrying defaulted loans until the recovery date. The cash flows were tested in relevant rating scenarios to determine if they were sufficient to pay interest and principal on the notes when due.

In terms of prepayments, Fitch modelled a high level that peaks at 20% under an ‘Asf’ scenario, and a low level at 2% per year. The cash flow analysis showed that the CE provided for the class A notes would be sufficient to withstand the default hurdles and losses that are commensurate with an ‘Asf’ rating.

Counterparty Risk

The transaction is not significantly exposed to a single counterparty, given the various and different entities involved with specific responsibilities. While Banco Santander holds the bank account, Banco Cooperativo is the paying agent and JPMorgan Securities Ltd the swap counterparty. Fitch considers that counterparty risk present in the structure has been adequately addressed via remedial actions detailed within the transaction documents.

Seller

Banco de Valencia, as seller, will continue acting as servicer of the collateral, as is the case for most Spanish RMBS transactions. To protect investors, if the seller is unable to continue servicing the collateral, the management company must appoint a replacement servicing company in accordance with Spanish securitisation law. The situations envisaged for servicer replacement are bankruptcy, intervention by the Bank of Spain or liquidation of the entity. In November 2011, Banco de Valencia requested the Spanish state’s Fund for Orderly Bank Restructuring (FROB) to substitute the board of directors. Since then, no payment disruptions have taken place.

As part of its rating process, Fitch performed an operational review of Banco de Valencia in June 2011 to assess the origination, underwriting and servicing capabilities of the seller. Additionally, the agency conducted a file review on a sample of ten files of the securitised pool to review the actual implementation of the underwriting standards on real cases. Please note that review visits and file sampling do not constitute any form of due diligence; Fitch does not perform due diligence but relies upon the accuracy of data provided. As a result of the review, Fitch considers that the assets were originated in accordance with Banco de Valencia’s origination policies.

Commingling and Payment Interruption Risk

Fitch believes the potential commingling risk of this transaction, in the event of a servicer disruption, is immaterial. This is based on the fact that payments made by the borrowers, as well as any other amounts to which the issuer is entitled as holder of the mortgage certificates, will be placed in the treasury account on a daily basis, thus reducing to a minimum the volume of collections that could commingled with the insolvency state of the defaulted servicer.

In case the servicer is insolvent, the asset collections and transfers to the treasury account are likely to be interrupted while alternative arrangements are made; this could produce short-term liquidity shocks that may lead to an interruption of payments to the notes. To mitigate such event, the seller has funded a cash deposit in the name of the issuer for an amount equal to expenses, net swap payments and interest on class A notes for a six-month period. These monies will be deposited at the treasury account and can only be used to mitigate the mentioned risk (ie, such funds cannot be used to provision for credit losses for example). The Gestora, on behalf of the issuer, will compute the dynamic deposits on a monthly basis.

Set-Off Risk

The issuer could be affected by the set-off rights of borrowers with deposits in accounts held with Banco de Valencia. However, this risk is mitigated as the seller commits itself in the documentation to remedying such circumstance if it arises at any point during the life of the transaction. The documents indicate that any amounts set-off by the borrowers will be compensated by the seller. Hence, no loss is expected to be borne by the issuer.

However, if the seller becomes insolvent, it cannot be relied upon to continue to compensate the fund for set-off amounts. Fitch derives comfort from Spanish law, where, upon the insolvency of the seller (or the borrower), or upon notification to the borrower of the assignment of the receivable, set-off is not valid. Hence, the only risk remaining is that of set-off being invoked and claimed prior to insolvency, but where the seller became insolvent before compensating the fund. Note that amounts that can be set-off do not relate to the entire mortgage loan amount, but rather to payments that are overdue, ie, the monthly instalments in arrears. The risk therefore remains limited and presents a very mild liquidity stress.

Account Bank and Paying Agent

Banco Santander ('A'/ Negative/'F1') acts as bank account where the Gestora, on behalf of the issuer, has opened a treasury account, while Banco Cooperativo Espanol ('BBB+'/Negative/'F2') acts as paying agent. The treasury account receives all incoming cash flows from the mortgage pool every day and transfers the moneys to the paying agent on each quarterly payment date. Amounts held at the treasury account receive a guaranteed interest rate equal to three-month Euribor.

Concerning the treasury account and the paying agent – and given that the maximum rating of the notes does not exceed 'A+sf' – if the ratings of Banco Santander or Banco Cooperativo Espanol are lowered below 'BBB+'/'F2', the Gestora will take one of the following steps within 30 calendar days: (i) obtain a first demand and unconditional guarantee from an entity rated at least 'BBB+'/'F2'; or (ii) replace either with an eligible counterparty rated at least 'BBB+'/'F2'. If, after such downgrade scenario, Banco Santander's or Banco Cooperativo's ratings returned to at least 'BBB+'/'F2', they could resume responsibilities as account bank provider and paying agent respectively.

Swap Counterparty

As stated in the section *Financial Structure and Cash Flow Modelling*, the issuer entered into two interest rate swap agreements with JP Morgan Chase, London Branch (not rated by Fitch) at closing. As of 2 December 2011, JP Morgan Securities Ltd (not rated) replaced JP Morgan Chase NA, London branch as swap provider. JP Morgan Securities Ltd is a subsidiary of JP Morgan Chase NA ('AA-'/Stable/'F1+') which has instrumented an irrevocable guarantee in favour of its subsidiary's role as swap provider.

Moreover, if JP Morgan Chase NA is downgraded below 'BBB+'/'F2'– and given that the maximum rating does not exceed 'A+sf' – it will take one of the following steps:

- find a replacement counterparty with a rating of at least 'BBB+'/'F2';
- find an entity rated at least 'BBB+'/'F2' to guarantee its obligations under the swap agreements; or
- cash- or security-collateralise its obligations in an amount satisfactory to existing Fitch criteria.

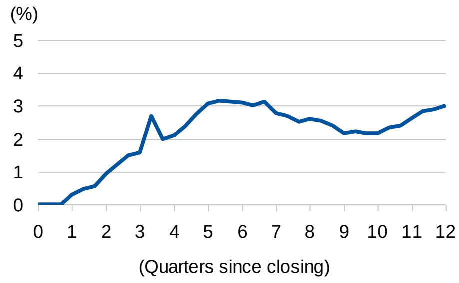
Performance Analytics

The ratings reflect the current risks to the transaction, while performance outside of expectations or the occurrence of certain events may trigger positive or negative rating actions. The on-going performance analysis of transactions forms an essential part of the Fitch rating process. A dedicated team handles the on-going monitoring and review of Fitch-rated RMBS transactions by assessing whether the transactions are performing as expected.

Figure 10

Valencia Hipotecario 5 FTA

3 months arrears over current balance

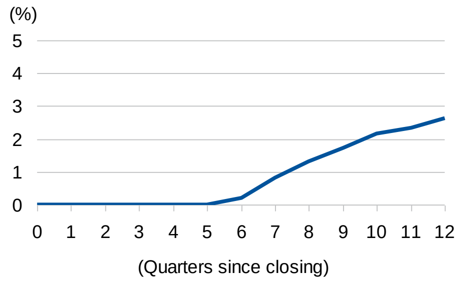


Source: Fitch and investor reports

Figure 11

Valencia Hipotecario 5 FTA

Cummulative defaults over original balance

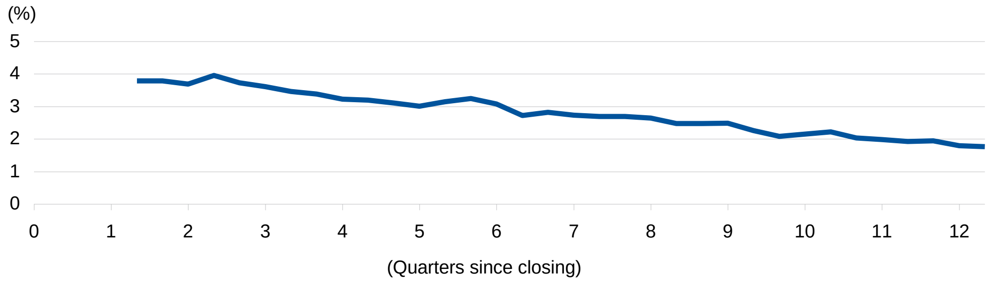


Source: Fitch and investor reports

Figure 12

Valencia Hipotecario 5 FTA

Annualysed constant prepayment rate (CPR)



Source: Fitch and investor reports

Fitch will monitor the transaction regularly and as warranted by events. Its structured finance performance analytics 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

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.