FitchRatings

Fitch Publishes New Criteria Assumptions for Spanish Mortgages; Spanish RMBS on RWN

Fitch Ratings has revised its criteria assumptions for Spanish residential mortgage portfolios in response to changing property market circumstances and the performance outlook. In particular, the revised assumptions reflect Fitch's findings that recoveries on defaulted mortgages have continued to decline, while the prospect of changes in the mortgage enforcement framework has increased the uncertainty surrounding defaults and recoveries in the longer term.

Following the assumption changes, Fitch has placed 220 tranches of Spanish RMBS on Rating Watch Negative (RWN). The agency has also maintained RWN on 80 tranches and has revised the Outlook on 47 tranch to Negative. A full list of rating actions and affected tranches can be found on www.fitchratings.com or by clicking the link above.

The assumptions in the revised criteria are applicable to the analysis of other asset portfolios secured by Spanish residential mortgages. Fitch does not expect to take rating action on covered bond (CvB) programmes or multi-issuer Cedulas Hipotecarias as a result of the assumption revisions. The levels of available overcollateralisation in these programmes are sufficient to absorb the lower recovery expectations. The assumption changes are also not expected to result in rating action on Spanish SME CLOs.

KEY RATING DRIVERS
- Increased Market Value Decline:
Information on the latest sales of properties taken into possession by lenders shows that sale prices achieved are further below those implied by applying the change in the home price index to the origination values. Fitch has increased its market value decline assumptions to reflect the higher discounts observed in forced sales. The 'quick sale adjustment' component of the market value decline has been increased to 45% from 35%. Th reduction in expected recoveries on defaulted loans is sufficiently large to potentially cause downgrades of the tranches on RWN.

- Extended Time to Recover:
Since December 2012, a temporary suspension of borrower eviction may be granted in certain circumstances, causing a delay in the mortgage enforcement process. Changes in the legal framework following a ruling of the European Court of Justice in March 2013 may also prolong the period to complete enforcements. The agency has therefore extended the length of time it is expected to take to recover on defaulted mortgages to 48 months from 36 months.

- Uncertainty over Changes to Mortgage Enforcement Process:
The agency's decision to revise the Outlook to Negative on 47 Spanish RMBS tranches reflects the uncertainty associated with changes to the mortgage enforcement framework, as a new mortgage law is currently bei drafted. In addition to changes already planned, the recent ruling by the European Court of Justice is likely to add to legislative initiatives to ensure future enforcements are deemed lawful. The eventual effects of framework changes on borrower payment behaviour, recovery timing and amounts are currently unclear and will be factored into Fitch's analysis as they emerge.

- Deteriorating Loan Performance:
The proportion of Spanish RMBS loans in serious arrears or default accelerated significantly over 2012, driven by unemployment and the expiry of unemployment benefits. In Fitch-rated transactions, loans in arrears by more than three months including net defaults reached 4.9% by the end of 2012, up from 3.6% a year earlier. Fitch's view is that the weak employment situation is not sufficiently offset by the low interest rate environm to prevent further increases in the proportion of loans in arrears and default across most transactions.

RATING SENSITIVITIES
- A change in legislation that materially changes mortgage borrower behaviour would cause the agency to revisit its assumptions and could have a negative effect on the ratings of associated securities.

- Home price declines beyond Fitch's expectations would limit expected recoveries, causing additional stress on portfolio cashflows. This would most severely affect those portfolios exposed to high loan-to-value ratio loans.

- Further stresses on borrowers could come from a rise in interest rates leading to increases in the volumes of loans in arrears and default.

Fitch will resolve the RWN following a full review of the transactions in the next four weeks. The review may result in some tranches being downgraded by multiple notches.

The report, "EMEA Criteria Addendum - Spain" replaces the existing report of the same name dated 24 July 2012. The criteria assumptions are published as an addendum to the "EMEA Residential Mortgage Loss Criteria" and should be read in conjunction with that report.

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