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Fitch Downgrades 2, Affirms 3 Classes of PYME Valencia 1, FTA; Assigns Outlooks

Ratings
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Fitch Ratings-London/Madrid-10 December 2008: Fitch Ratings has today downgraded the ratings of two classes and affirmed three classes of PYME Valencia 1, FTA, and simultaneously assigned or maintained rating Outlooks, as follows:

Class A2 (ISIN ES0372241002) affirmed at 'AAA'; assigned a Negative Outlook
Class B (ISIN ES0372241028) affirmed at 'A'; assigned a Negative Outlook
Class C (ISIN ES0372241051) downgraded to 'BB' from 'BBB'; assigned a Negative Outlook
Class D (ISIN ES0372241036) downgraded to 'B' from 'BB'; Negative Outlook maintained
Class E (ISIN ES0372241044) affirmed at 'CC'

The review was prompted by an increase in the amount of delinquent loans in the transaction and concerns about Spain's macroeconomic environment. As of 30 September 2008, 90+ day delinquencies stood at 2.7% of the current portfolio. Further, the portfolio is highly concentrated in real estate and related sectors with the current exposure at 59.7%, and the largest geographical region is Valencia at 60.7%. The transaction is also exposed to obligor concentration with the largest obligor accounting for 2% of the portfolio and the top five obligors totalling EUR50.9m or 9.2%. The transaction closed in 2007 and has not benefited from de-leveraging to the same degree as older vintage transactions. The current portfolio is 64.9% of the initial portfolio balance, which has led to a small increase in credit enhancement on the notes. The reserve fund of EUR15.3m provides 2.7% of credit enhancement. While current levels of credit protection for classes A2 and B remain sufficient to maintain the current rating, the transaction is exposed to the delinquency pipeline, and these notes have thus been assigned Negative Outlooks. Fitch's analysis of the delinquency pipeline and updated default forecast for the current portion of the portfolio indicates that the credit protection for classes C and D has declined markedly which is why the notes have been downgraded to below investment grade with Negative Outlooks as noted above.

Fitch assigned Negative rating Outlooks between May and September 2008 to 19 tranches issued by Spanish small- and medium-sized enterprise (SME) collateralised debt obligation (CDO) transactions due to a combination of declining performance trends and the worsening Spanish macroeconomic environment. In a special report published on 8 May 2008, entitled "Rating Outlooks in Spanish SME CDOs", Fitch discussed why the agency had a negative view for the next one-to-two years and highlighted macroeconomic trends and concerns which, the agency believes, increase the downgrade risk for such notes over the long term.

Since then, there has been a notable increase in delinquencies. While significant losses have yet to materialise, Fitch expects further deterioration due to the downturn in the Spanish economy and the significant exposure of the transaction to the real estate and related sectors. While recent declines in interest rates and augmented collection efforts may relieve some degree of stress in the portfolio, Fitch expects performance to weaken further over the near-term due to deteriorating macroeconomic conditions and growing stress in the real estate and construction sectors. Given these expectations, the transaction was reviewed to determine if the levels of credit protection were sufficient to maintain the current ratings.

In the analysis undertaken, assumptions on probability of default (PD) and loss severity were made with regards to current delinquencies as well as the performing portfolio. With respect to default probability, the base assumption on the current portion of the portfolio was revised upward to reflect the non-investment grade nature of underlying obligors and to consider how the portfolio or loans could perform through-the cycle. This resulted in an increase in the base default probability to approximately 10-15%, which was then adjusted to reflect the remaining weighted average life of the portfolio. The base case PD was further adjusted to account for the existing portfolio delinquency pipeline, with loans in later state delinquency buckets assigned progressively higher default probabilities (up to 100% for loans greater than six months in arrears). On the recovery side, Fitch assumed the 'BB' recovery from the initial rating analysis. These updated PD and recovery assumptions were used to determine an updated loss expectation and then compared against existing subordination available for each tranche, with minimum coverage ratios of the updated expected loss driving the actions noted above. Seasoning, excess spread, as well as industry and obligor concentration risk also factored into Fitch's credit view.

This transaction is a cash flow securitisation of secured and unsecured loans granted by Banco de Valencia ('A-'((A minus))/'F2'/Outlook Stable) to SMEs in Spain. PYME Valencia 1, FTA, a limited liability SPV incorporated under Spanish law, will be legally represented and managed by Europea de Titulizacion, SGFT, SA, whose activities are limited to the management of securitisation funds.

Further commentary and performance data on these transactions are available on the agency's subscription website, www.fitchresearch.com.

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