



**Rating Action: Moody's downgrades two Spanish ABS from Banco de Valencia due to operational risk**

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London, 16 December 2011 -- Moody's Investors Service has today downgraded the ratings of two senior tranches in two Spanish asset-backed securities (ABS) transactions, PYME VALENCIA 1, FTA and PYME VALENCIA 2, FTA, which are serviced by Banco de Valencia S.A. (Ba2/NP/E+). The downgrades reflect operational risk concerns. The rating action concluded the rating reviews of the two transactions.

As part of the review, Moody's also assessed the effect of the increased commingling risk in these transactions since the downgrade of Banco de Valencia to Ba2 on 28 October 2011.

A detailed list of the ratings affected by today's action appears at the end of this press release.

**RATINGS RATIONALE**

Today's rating action reflects the lack of back-up servicer (BUS) arrangements in place to support payments on the rated tranches in the event of servicer disruption.

**--LACK OF BUS ARRANGEMENT**

Moody's notes that the transactions are exposed to operational risk as there is no BUS arrangement in place to deal with a potential servicer disruption. While PYME VALENCIA 2, FTA includes a trigger to appoint a BUS upon the loss of the servicer's Baa3 rating, no BUS has yet been appointed.

However, a mitigant to payment disruption risk is the role of Europea de Titulización, the management company, that will coordinate the appointment of a replacement servicer if Banco de Valencia is not able to perform its duties. The management company also acts as an independent cash manager and will be able to use available funds, including the reserve fund, to support timely payments on the notes in case of a temporary servicer disruption.

In taking today's rating action, Moody's has considered (i) the level of liquidity available in the transactions; and (ii) the role of the management company acting as (a) independent cash manager; and (b) BUS facilitator to help support continuity of payments in case of servicer default.

**--LACK OF LIQUIDITY IN PYME VALENCIA 1, FTA**

Moody's downgraded the senior notes of PYME VALENCIA 1, FTA to A2 (sf) because the transaction does not benefit from any liquidity source. The reserve fund is fully depleted.

**--SUFFICIENT LIQUIDITY AVAILABLE IN PYME VALENCIA 2, FTA**

PYME VALENCIA 2, FTA benefits from a large principal cash reserve of EUR84.4 million and an interest cash reserve of EUR2.7 million, both deposited in Banco Popular Espanol, S.A. (A2/P-1), representing, respectively, 35.5% and 1.1% of the current pool balance.

Moody's believes that the current liquidity level in this transaction is sufficient to support interest payments on the notes in the event of a disruption in collections. In addition, the reserve fund currently represents 55.6% of the senior notes balance, which strongly mitigates a potentially prolonged absence of securitised loan servicing. Such an extended period without loan servicing could result in additional losses on the pool. As a result, Moody's concluded with a maximum achievable rating of Aa3(sf) for the senior

notes of PYME VALENCIA 2, FTA 2.

#### --LIMITED IMPACT OF THE INCREASE IN COMMINGLING RISK

In addition, Moody's has concluded that the increased commingling risk on these two transactions, following the downgrade of Banco de Valencia, did not affect the ratings of the notes, given the current credit enhancement levels versus the ratings on the notes.

#### --SWAP COUNTERPARTY REPLACED IN PYME VALENCIA 1, FTA

For PYME VALENCIA 1, FTA, BBVA (Aa3/P-1/B-) replaced Banco de Valencia as swap counterparty.

There is no swap in place in PYME VALENCIA 2, FTA.

#### --POOR PERFORMANCE IN PYME VALENCIA 2, FTA

As part of its review, Moody's reassessed the portfolio quality of PYME VALENCIA 2, FTA due to poor performance. In contrast, PYME VALENCIA 1, FTA performance remained in line with expectations.

As of October 2011, cumulative 90+ day delinquencies for PYME VALENCIA 2, FTA stood at 13.8% of the original balance compared with a 15%.8 assumption over the life of the transaction. Historically, this transaction has under-performed Moody's Spanish SME delinquency index ("Spanish SME Indices - September 2011"). As of September 2011, 90- to 360-day delinquencies represented 4.22% of the current pool balance, compared with the weighted average index of 2.75%.

#### --KEY REVISED ASSUMPTIONS IN PYME VALENCIA 2, FTA

Moody's used the "top-down" approach to derive the default-rate assumption, whereby an average through-the-cycle rating for Spanish SMEs is determined and the rating is then adjusted on a loan-by-loan basis by considering various factors, including the borrower sector, repayment profile and the broader economic environment. As part of its review, Moody's considered the exposure of the transaction to the real estate sector (46% of the current pool as of September 2011 according to Moody's classification). As a result of the above, Moody's assumed the default probability of SME debtors to be equivalent to a rating in the single B-range for debtors operating in the real estate sector and in the low Ba-range for the non-real-estate debtors. At the same time, Moody's estimated the remaining weighted average life of the portfolio to equal 5.2 years. Consequently, the revised cumulative mean default assumption for this transaction has increased to 24% of the current portfolio balance (corresponding to 25% of original portfolio balance).

Given that the pool is less granular (with an effective number of borrowers of 351), Moody's used a Monte Carlo simulation in CDOROM to derive the gross default distribution. As a result, Moody's revised the coefficient of variation of its default distribution to 42%. Moody's assumptions for the average recovery rate and constant prepayment rate (CPR) remain unchanged at 45% and 5%, respectively.

Although the quantitative rating model outcome is still equivalent to Aaa, the downgrade of the PYME VALENCIA 2, FTA senior notes reflects the lack of a BUS arrangement. As such, Moody's today downgraded the class A notes to Aa3 (sf) from Aaa (sf). The model outcome is consistent with current ratings on subordinated notes.

For PYME VALENCIA 1, FTA, key modelling assumptions, sensitivities, cash-flow analysis and stress scenarios have not been updated as today's rating action has been primarily driven by the lack of liquidity and the lack of a BUS arrangement.

Uncertainty mainly stems from the lack of a back-up servicer in these transactions. Banco de Valencia was intervened by Bank of Spain as of 21 November 2011. Although this helps mitigate servicer disruption in the short term, there is high uncertainty as of the future of the entity. If the rating of Banco de Valencia

is downgraded further while no back-up agreement is in place, the ratings would be negatively affected.

As noted in Moody's comment 'Rising Severity of Euro Area Sovereign Crisis Threatens Credit Standing of All EU Sovereigns' (28 November 2011), the risk of sovereign defaults or the exit of countries from the Euro area is rising. As a result, Moody's could lower the maximum achievable rating for structured finance transactions in some countries, which could result in rating downgrades.

The methodologies used in these ratings were "Moody's Approach to Rating CDOs of SMEs in Europe" published in February 2007, and "Moody's Approach to Rating Consumer Loan ABS Transactions" published in July 2011. Please see the Credit Policy page on [www.moody.com](http://www.moody.com) for a copy of these methodologies.

During the review of PYME VALENCIA 2, FTA, Moody's used its excel-based cash flow model, Moody's ABSROM™, as part of its quantitative analysis of the transaction. Moody's used CDOROM to model the cash flows and determine the loss for each tranche. The Moody's CDOROM™ is a Monte Carlo simulation, which takes the Moody's default probabilities as input.

Issuer: PYME VALENCIA 1, FTA

...A2, Downgraded to A2 (sf); previously on Mar 25, 2011 Aa3 (sf) Placed Under Review for Possible Downgrade

Issuer: PYME VALENCIA 2, FONDO DE TITULIZACIÓN DE ACTIVOS

...A, Downgraded to Aa3 (sf); previously on Jun 30, 2011 Aaa (sf) Placed Under Review for Possible Downgrade

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