

SME CDOs  
Italy  
New Issue

# BPM Securitisation 2 S.r.l.

Series 2009-1

## Analysts

Alessandro Cipolla  
+39 02 879 087 238  
alessandro.cipolla@fitchratings.com

Nick Apsley  
+44 20 7417 6293  
nicholas.apsley@fitchratings.com

Lars Jebjerg, PhD  
+44 20 7417 6289  
lars.jebjerg@fitchratings.com

## Performance Analytics

Jeffery Cromartie  
+44 20 7664 0072  
jeffery.cromartie@fitchratings.com

## Corporates

Julian Crush  
+44 20 7682 7370  
julian.crush@fitchratings.com

Adriano Rampazzi  
+44 20 7682 7346  
adriano.rampazzi@fitchratings.com

## Related Research

- [Global Rating Criteria for Corporate CDOs \(Apr 08\)](#)
- [Global Criteria for Cash Flow Analysis in Corporate CDOs \(Apr 08\)](#)
- [Commingling Risk in Structured Finance Transactions \(Jun 04\)](#)
- [Counterparty Risk in Structured Finance: Qualified Investment Criteria \(Sep 07\)](#)
- [Special Purpose Vehicles in Structured Finance Transactions \(Jun 06\)](#)
- [BPM Securitisation 2 S.r.l. \(Jul 06\)](#)
- [Region of Lombardy \(Sep 08\)](#)

## Rating

Class	Amount (EURm)	Final Maturity	Credit Enhancement <sup>b</sup> (%)	Rating <sup>a</sup>	Outlook
A	923.95	April 2041	29.4	AAA	Stable
B	377.88	April 2041		n.r.	
<b>Total issuance</b>	<b>1,301.83</b>				

The ratings are based on information provided by the issuer as of the closing date. Ratings are not a recommendation to buy, sell or hold any security. The offering circular and other material should be reviewed prior to any purchase

<sup>a</sup> Class A is rated for the ultimate return of principal and the timely payment of interest, according to the term and conditions of the notes

<sup>b</sup> Credit enhancement in the form of subordination only

## Transaction Summary

Under this balance sheet securitisation, BPM Securitisation 2 S.r.l. (the issuer) has issued floating-rate notes secured by a EUR1,285.1m portfolio of loans to Italian small- and medium-sized businesses (SMEs). The loans were originated by Banca Popolare di Milano S.c. a r.l. (BPM, rated 'A'/'F1'/Stable) in its normal course of business prior to being transferred to the issuer. The issuer is a special-purpose vehicle (SPV) incorporated in accordance with the Italian Law of 30 April 1999, No.130.

## Key Rating Drivers

- **Defaults:** the rated notes have sufficient credit enhancement to withstand a nine-fold increase to the originator's historical average default rate with recovery rates of about one-third of the originator's historical average.
- In addition, the rated notes benefit from substantial de-leveraging over the first two years due to amortisation (the portfolio is scheduled to de-leverage by 23% during the first year and 17% in the second year), while interest available funds (IAF) can also be used to accelerate the amortisation of class A notes via a Principal Deficiency Ledger (PDL).
- **Industry Concentration:** the largest industry is real estate and accounts for about 43% of the portfolio notional. Real estate concentration has been accounted for in Fitch Ratings' analysis by the assumed correlation level and by stress-testing the rating for shocks in the assumed portfolio default rates (refer to the "Rating Sensitivity" section below for more details).
- **Single Obligor Concentration:** the rated notes have sufficient subordination to withstand a default of the largest 10 obligors, which represent 12% of the portfolio notional.
- **No Hedging Agreement:** no interest rate hedging agreement has been put in place for this transaction, leaving the SPV exposed to interest rate basis and reset risk. This has been taken into account in Fitch's cash flow analysis of the transaction (refer to the "Cash Flow Modelling" section below for more details).
- **Exposure to the originator:** BPM fulfils the roles of servicer and collection account bank. The transaction documents include mitigation, such as counterparty replacement within 30 days of a downgrade below 'F1', which complies with Fitch's counterparty criteria. Fitch's counterparty criteria are currently being reviewed (please refer to the *Counterparty Risk* section below for more details on this). However, the class A notes would be vulnerable if there was a sudden and direct default of BPM during this period. BPM currently has a Support Rating of '3' and is one of the eight largest Italian domestic banks.

The ratings are based on the credit enhancement provided to the rated notes and the structural features of the transaction. The rated notes benefit from 29.4% subordination on the closing date and IAF can be trapped by a PDL mechanism for the benefit of the rated notes until these have been redeemed in full. In the absence of a hedging agreement, Fitch modelled interest rate basis and reset risk and this resulted in no benefit being given to excess spread in its analysis (please refer to the *Cash Flow Modelling* section below for more details); this approach is likely to prove conservative.

Model-only sensitivity tests imply that the rated note is likely to remain stable against mild changes in individual key assumptions and changes to multiple factors. Moderate or severe changes to assumptions imply negative potential rating actions in the 'AA' category.

Fitch surveils the transaction based on a fuller assessment of all relevant factors. Changes to individual assumptions may be exacerbated, or offset, by other factors and a downgrade may or may not occur.

## Rating Sensitivity<sup>1</sup>

The rated notes have sufficient subordination - without accounting for the additional protection afforded by PDL, prepayments and scheduled de-leveraging of the securitised portfolio - to withstand losses of 28.5 times the originator's historical average loss experience, or the default of the largest 10 obligors without taking losses. The notes also have enough subordination to withstand a nine-fold increase to the originator's historical average default rate with recoveries of about one-third of the originator's historical average.

## Rating Sensitivity to Defaults<sup>2</sup>

The structure is robust to increases in default probability beyond the originator's average historical experience. Model results, when instantaneously increasing the input portfolio default rate by 10% or 25%, show a one notch model-implied downgrade:

### Rating Sensitivity to Defaults

	Class A
Fitch base default rate assumption (2.9% in one year, 14.5% over four years)	AAA
A 10% increase in the assumed portfolio default rate (3.2% in one year: 6.1 times originator's historical rate, 16.0% over four years: 4.9 times originator's historical rate)	AA+
A 25% increase in the assumed portfolio default rate (3.6% in one year: 6.9 times originator's historical rate, 18.1% over four years: 5.7 times originator's historical rate)	AA+

Source: Fitch

## Rating Sensitivity to Correlation

The model results show reasonable robustness to increases in assumed correlation. A 4% and 8% absolute base correlation increase (38% and 88% stress respectively to the correlation assumption) results in a two and four notch model-implied downgrade:

### Rating Sensitivity to Correlation

	Class A
Fitch base correlation assumption (average portfolio correlation 8%)	AAA
A 4% absolute increase to base correlation (average portfolio correlation 11%, relative parameter stress of 38%)	AA
A 8% absolute increase to base correlation (average portfolio correlation 15%, relative parameter stress of 88%)	A+

Source: Fitch

<sup>1</sup> These sensitivities only describe the model-implied impact of a change in one or more of the input variables to levels more conservative than those factored in the 'AAA' stress scenario. 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

<sup>2</sup> This section provides a greater insight into model-implied rating sensitivities. The results in this section show one potential outcome; however, in reality, the transaction is exposed to multiple dynamic risk factors

**Rating Sensitivity to Recovery Rates**

The rated notes are not too sensitive to changes in recovery rates. Haircutting the assumed recovery rates by 25% or 50% (to approximately 1/4 and 1/6, respectively, of the originators historical recoveries) result in a one notch model-implied downgrade:

**Rating Sensitivity to Recovery Rates**

	Class A
Fitch base recovery rate assumption (portfolio weighted average recovery rate 24%)	AAA
A relative recovery rate haircut of 25% (portfolio weighted average recovery rate 18%)	AA+
A relative recovery rate haircut of 50% (portfolio weighted average recovery rate 12%)	AA+

Source: Fitch

Model-only sensitivity tests imply that the rated note remains in the 'AA' category in a mild combined stress; however, if the high or severe combined stress were to materialise immediately it could suffer a downgrade to 'A+' or 'BBB+'.

**Rating Sensitivity to Shifts in Multiple Factors**

The table below summaries the rating sensitivity to stressing multiple factors immediately and concurrently. Three scenarios are evaluated to demonstrate the sensitivity of the rating to varying degrees of stress to the expected level of defaults, recoveries and correlation. The sensitivities Fitch uses are based on inputs which are more conservative than those assumed to assign its rating, which in turn are more conservative than historical data provided by the originator.

Please refer to the preceding page for more information on each stress component.

**Rating Sensitivity to Shifts in Multiple Factors**

	Class A
Original rating	AAA
Mild stress: default rate increase of 10%, recovery rate haircut of 10% and base correlation increase of 4%	AA-
High stress: default rate increase of 25%, recovery rate haircut of 25% and base correlation increase of 4%	A+
Severe stress: default rate increase of 25%, recovery rate haircut of 50% and base correlation increase of 8%	BBB+

Source: Fitch

The model-implied results of the combined stresses show that class A, with an initial rating of 'AAA', would suffer a downgrade of three notches in a mild stress scenario, a downgrade of four notches in a high stress scenario, and a downgrade of seven notches in a severe stress scenario. These results assume that the stress materialises immediately, before the transaction has benefited from de-leveraging or PDL.

**Model, Criteria Application and Data Adequacy**

BPM provided historical default, delinquency, prepayment and recovery data for the period 1997-2007. Fitch also relied on its European and Italian SME default rate and recovery rate benchmarks, which are, amongst other sources, based on data from Bank of Italy.

Default data has been supplied based on a definition of default which includes both sofferenze (hard defaults) and 180 days past due (dpd), which is also the default definition used in the transaction. This data shows a fairly stable trend.

BPM supplied internal credit scores and expected probabilities of default (PD) for the obligors in the portfolio. These were considered in the qualitative assessment and found to show lower expected default rates than the values assumed by Fitch. These were not relied on directly in Fitch's quantitative analysis; however, Fitch will use this information in its ongoing surveillance of the portfolio.

Asset PDs were initially derived from the originator's historical data; however, Fitch also took into account the credit opinions derived by its Corporate analysts for the largest 19 obligors (accounting for 17% of the portfolio notional) on the basis of their financial statements. The portfolio default rate assumptions used in the final analysis compare unfavourably with Fitch's Italian PD benchmarks.

Recovery rate assumptions are based on Fitch's benchmarks, which imply lower recovery rates than the historical average recovery rate achieved by BPM.

Several models were used in assigning the ratings to the notes. Fitch's Portfolio Credit Model (PCM) version 2.1.0 was used in the analysis of the asset portfolio. Fitch's Proprietary Cash Flow Model was used to further analyse the transaction's cash flows and liability structure. Fitch's Cash Flow Model was customised to account for the specific structure of the transaction. For further information, please refer to section "*Portfolio Credit Analysis*".

### **Transaction and Legal Structure**

The transaction is a balance sheet securitisation of secured and unsecured loans to small- and medium-sized businesses in Italy, predominantly north west Italy. The loans have been transferred to BPM Securitisation 2 S.r.l., an SPV incorporated under law n.130 enacted in April 1999 (the Italian securitisation law), prior to the transaction closing.

In June 2006 the issuer carried out a securitisation of residential mortgage loans (for more detail see the report "*BPM Securitisation 2*" referred to on page 1 under the "*Related Research*" section), and may purchase and securitise further portfolios of loans in addition to the portfolios already purchased. Under the terms of the Italian securitisation law, the assets relating to each securitisation transaction will, by operation of law, be segregated for all purposes from all other assets of the company that purchases the assets.

The issuer is owned 100% by Stichting Vendrburg, a Dutch foundation.

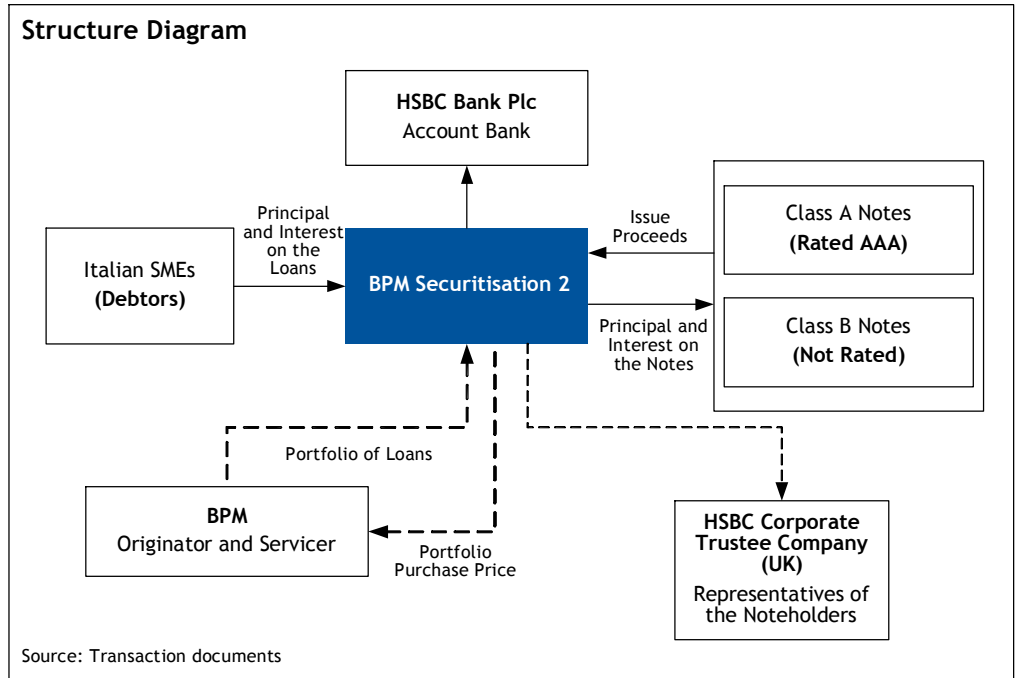
### **Disclaimer**

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.

Interest available funds can be used to accelerate the amortisation of the notes via a principal deficiency ledger (PDL); principal available funds can be used to cover interest shortfalls via the Interest Shortfall Amount (ISA) item of the principal priority of payment, as detailed below.

### **Interest Priority of Payment**

1. taxes, fees and expenses;
2. class A notes' interest;
3. class A PDL;
4. cash reserve;
5. class B notes' interest;
6. class B PDL;
7. junior payments.



### Principal Priority of Payment

1. Interest shortfall amount;
2. class A notes' principal;
3. class B notes' principal;
4. junior payments.

### Principal Lock-Out Period

If the issuer redeems the notes in whole or in part in the first 18 months after issuance, it will be required to pay a tax equal to 20% of the interest accrued on repaid principal at the repayment date. For this reason, no principal repayments will be made in the first 18 months after closing (ie up to the payment date falling in January 2011). During this lock-out period, principal repayments due on the notes will be deposited in the transaction account held in the name of the issuer at the account bank.

### Events of Default

Events of default under the notes include:

- non-payment of interest or principal on class A notes by the issuer on the due date or within five business days from the due date;
- issuer defaults in the performance of its obligations for 30 days;
- breach of representations and warranties by the issuer;
- insolvency of the issuer;
- it is or will become unlawful for the issuer to perform or comply with its obligations.

### Asset Analysis

The collateral at closing comprises 10,725 assets from 9,322 obligors. All assets have been originated by BPM in the course of its normal business.

Each asset must comply with the eligibility criteria at the time of inclusion.

### Portfolio Characteristics

**Current Portfolio:**  
EUR1,285.10m  
**Mortgage Secured:** 66%  
**Fixed/Floating/Mixed:**  
13.4%/80.9%/5.7%  
**WAS (Floating Only):**  
120bps  
**WAC (Fixed Only):** 5.71%  
**Number of Obligor:** 9,322

### Key Information

**Type of Assets:** secured loans to small- and medium-sized businesses in Italy  
**Weighted Average Months to Maturity:** 87  
**Max Months to Maturity:** 305  
**Principal Lock-out Period:** 18 months

## Eligibility Criteria

Under Italian securitisation law, the portfolio eligibility criteria must be applied to all assets on the originator's book and the criteria must be made public in the Official Gazette. For this securitisation, receivables arise from loans that, among others:

- have been granted by BPM to companies or individuals resident in Italy in relation to their commercial operations and are governed by Italian law;
- are denominated in euro, are fully drawn, and mature no later than 31 March 2034;
- are unsecured or mortgage-secured loans;
- in case of mortgage loans, are secured by an economic first ranking mortgage over property located in Italy;
- have paid at least one instalment, have no instalments in arrears for over 90 days, and have been granted to debtors that are not classified as non-performing (in sofferenza) by BPM;

Loans excluded from the securitisation portfolio include loans granted to public entities, debtors classified as non performing (in sofferenza) by BPM, employees of BPM or any company belonging to the BPM group, and loans stipulated in accordance with any regulation foreseeing facilities or public contributions.

If further loans on BPM's balance sheet are found to be eligible under the above criteria - due to error in the initial asset selection or transfer process - then these assets will be automatically transferred to the securitisation, and any payments that may be due by the issuer to BPM following such transfer will rank junior to the rated notes.

## Default Definition

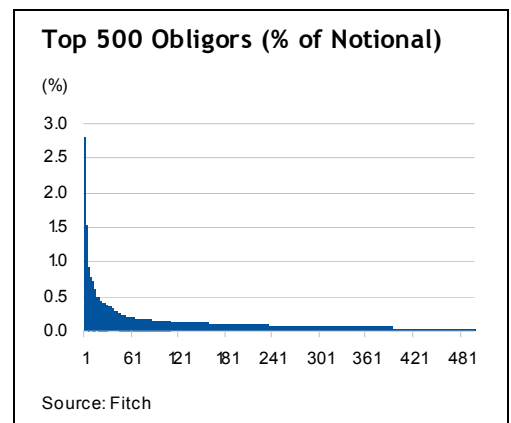
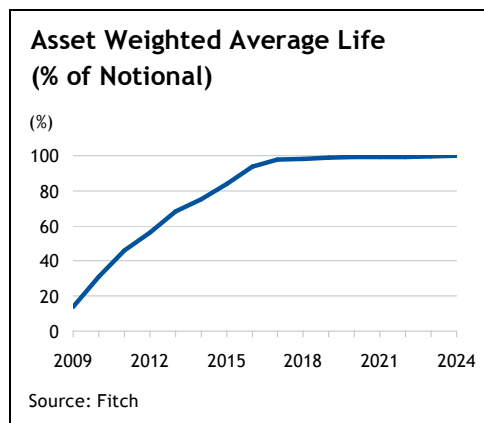
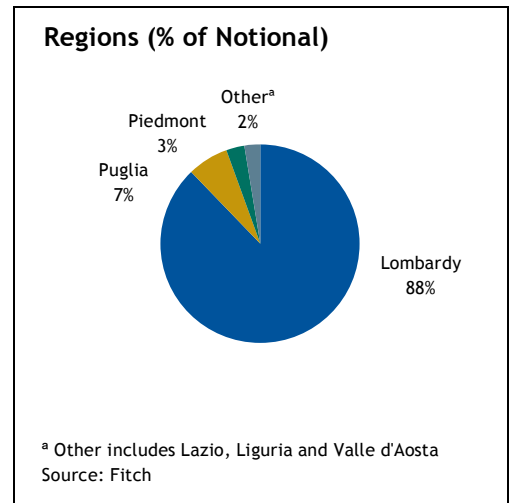
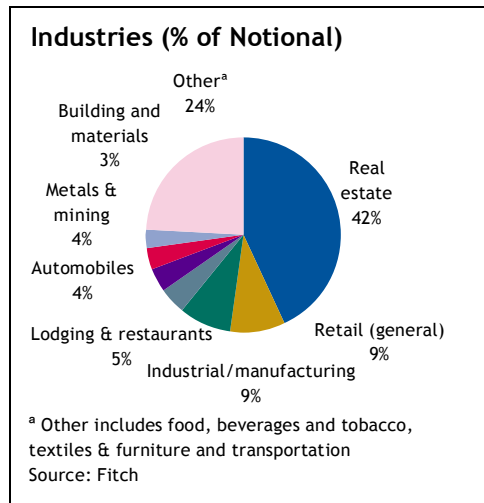
Defaulted loans are loans: (a) having at least (i) one annual instalment which is past due and unpaid for more than 180 days, (ii) two semi-annual instalments which are past due and unpaid, (iii) three quarterly instalments which are past due and unpaid, or (iv) six monthly instalments which are past due and unpaid; or (b) in relation to which the relevant debtor has been classified as non performing (in sofferenza) by BPM. Note that 52% of the portfolio consists of loans paying monthly instalments, 33% pay quarterly and 15% pay semi-annually.

No assets were in default on the closing date; however, 1.5% were in arrears by 90 days or less.

## Portfolio Stratification

All loans are granted to borrowers based in Italy with a high concentration in north west Italy, especially in the Lombardy region (88%). For an overview of the economic profile of this region please refer to the "*Region of Lombardy*" report published in September 2008 by Fitch and listed on page 1 under the "*Related Research*" section.

Industry concentration is high. The three largest sectors account for 61% of the portfolio by volume; 43% of the portfolio is in real estate, 9% in retail, and another 9% is in industry and manufacturing.



As can be seen in the Asset Weighted Average Life chart above, the portfolio is scheduled to de-leverage quickly (by 23% during the first year and 17% in the second year).

The portfolio, although granular, has some obligor concentration. The largest obligor accounts for 2.8% of the portfolio notional, while the ten largest obligors collectively represent 12.1% of the portfolio.

### Portfolio Credit Analysis

Fitch modelled most assets in the portfolio with a one-year default probability of 0.5% (comparable to the historical performance of 'BBB-'/'BB+' rated assets), which was derived on the basis of the originator's historical default data, to which a 17% long-term mean (LTM) adjustment was applied (based on historical default data sourced from the Bank of Italy) in order to better capture the average default rate expected over a full economic cycle. This approach was not applied to the 19 largest obligors that comprise 17% of the initial pool; these assets were assessed individually by Fitch's corporate ratings group, mainly based on information sourced from their financial statements. Several of the largest obligors were found to be distressed or showed poor financial performance, hence the assessment indicated a lower credit quality (between 'CCC-' and 'CC') for them compared to the granular part of the portfolio. This was reflected in Fitch's analysis and reduced the weighted average portfolio credit quality to 'B+'.

## Default Rates (%)

Term	1 year	4 years
Fitch assumption	2.9	14.5
Originator default rate, with LTM adjustment	0.5	3.3
Originator reported historical default rate	0.4	2.8

Source: Fitch

Fitch stressed its base assumptions for the five largest obligors, which represent about 8.2% of the portfolio: these obligors were modelled with recovery rates 25% below the base case (ie 0.75 times the base recovery rate) and with correlation increased by 50% (absolute amount), as is consistent with the Obligor Concentration Uplift (OCU) stress, pursuant to Fitch's corporate CDO criteria (see "*Global Rating Criteria for Corporate CDOs*", published April 2008).

Sixty-six percent of the assets are secured on first ranking mortgages or equivalent security. Fitch has been provided with collateral information for each asset. The agency applied lower recovery rates in its analysis compared to the originator's historical experience.

The use of higher default rates and lower recoveries compared to BPM's historical data was motivated by a number of factors, including:

- while the data provided by BPM covers a period of ten years, data from the Bank of Italy shows that the Italian default rate peaked in the early 1990s; this stress (referred to as long-term mean adjustment) is incorporated in Fitch's assumptions;
- the average rate inferred from historical default data provided by the originator is significantly lower than the agency's Italian SME benchmark default rate. Fitch does not believe that SME obligors *on average* will behave like investment grade companies and hence gave limited credit to the historical default data provided by BPM (this decision was also made in light of the result of the above mentioned assessment conducted by Fitch's corporate ratings group on the largest obligors);
- the 19 largest obligors account for 17% of the portfolio notional. Fitch has reviewed financial information for these obligors and applied additional stresses in its analysis;
- recovery rate studies indicate average recoveries for SME loans that are lower than those achieved by BPM historically. Fitch has assumed base case recoveries closer to the market average level, whilst differentiating by type and level of collateral for each loan; the agency further reduced those levels to reflect the fact that recoveries may be substantially below historical averages in a 'AAA' stress.

The following section shows the result of the asset analysis.

## Asset Rating Default Rate

### PCM Results

Rating stress (%)	Rating default rate (RDR)	Rating loss rate (RLR)
'AAA'	31	23

Source: Fitch

In its credit analysis, the agency used the Fitch Portfolio Credit Model (PCM) to determine the hurdle default rate (rating default rate, RDR) for the 'AAA' rated note. The PCM is Fitch's main quantitative portfolio analysis tool. The model simulates the joint default behaviour for a portfolio of credit exposures, taking into

account asset-specific PDs, recovery rates, and default correlations. See the reports, “*Global Rating Criteria for Corporate CDOs*” and “*Global Criteria for Cash Flow Analysis in Corporate CDOs*”, both dated 30 April 2008, for further details.

## Cash Flow Modelling (Liability Analysis)

In the second step of Fitch’s analysis, the structural protection and the excess spread were analysed in a customised proprietary cash flow model. The resulting breakeven default rate (which shows the maximum default rate the rated notes could withstand without a loss) is compared to the above-mentioned hurdle rate produced by the PCM. The breakeven default rate must be above the PCM hurdle rate for a rating to be assigned.

While the rated notes pay six-month Euribor the loans included in the collateral portfolio include fixed-rate (accounting for 13.4% of the portfolio), floating-rate (80.9%) and mixed-rate loans<sup>3</sup> (5.7%). Floating-rate loans are mainly referenced to monthly, quarterly or semi-annual averages of three-month EURIBOR. As no hedging agreement has been put in place for this transaction, the SPV is exposed to both basis and reset interest rate risk. Fitch took these risks into account by means of a constant reduction of the spread payable on the loans; the size of this reduction was determined on the basis of a time series analysis of the historical average and standard deviation of the differences between the interest rate indexes on the asset and liability sides of the SPV. In addition, Fitch also applied a one year stress of a 100bps to mitigate the risk of a substantial, temporary mismatch between the indexes on the asset and liability sides of the SPV (which Fitch will refer to as a ‘super-stress on basis risk’). This resulted in no credit being given to excess spread. Moreover, Fitch applied a weighted average margin compression stress, where defaults and prepayments are applied to the highest yielding assets first.

Based on historical data provided by the originator, Fitch determined a base case annual prepayment rate equal to 4%, which was factored in to its cash flow analysis of the transaction. However, Fitch also considered fast and slow prepayment scenarios, where the prepayment rate is respectively twice or half as large the base case rate. Claw-back risk on prepayments, pursuant to article 65 of the Italian bankruptcy law, was not deemed to be material.

The analysis showed that the protection provided for class A notes would be sufficient to withstand the default hurdles/losses produced by the PCM model for the ‘AAA’ rating. The simulations also highlighted the sensitivity of the transaction to defaults occurring early in the transaction life - as the assumed recovery lag for Italy is longer than for other Western European jurisdictions - and to increasing interest rates, when the cost of funding of the transaction increases while excess spread remains limited, due to early defaults. However, as a result of the above-mentioned super-stress on basis risk, a scenario where defaults are evenly distributed over the life of the transaction turned out to be more stressful than a scenario where defaults are front-loaded. On the other hand, assuming back-loaded default timings, expected amortisation on the portfolio significantly reduces the class A note principal before defaults begin to disrupt class A cash flows. Default timing scenarios have been determined based on Fitch’s, “*Global Criteria for Cash Flow Analysis in Corporate CDOs*”, published April 2008.

The driving Fitch default scenarios, break-even default rates, and the cushions for the base cases are highlighted in the table below. Note that the cushion noted in the table also results from the transaction structure, whereby interest available funds can be used to accelerate the amortisation of class A notes via a principal deficiency ledger; this helps maintain timely interest on the class A notes and also

<sup>3</sup> Mixed rate loans include fixed rate loans with a voluntary or compulsory future switch to floating rate and floating rate loans with a voluntary future switch to fixed rate.

contributes to the faster repayment of class A principal in a high default environment (compared to using just principal proceeds).

### BPM Securitisation 2 S.r.l. Break-Even Default Rates

Class	A
Expected rating	AAA
Breakeven default rate (BDR) (%)	31.1
PCM default hurdle (%)	30.7
Default cushion (%)	0.4
<b>Driving scenario</b>	
Default timing	Evenly
Prepayment	Slow
Euribor	Rising

Source: Fitch

### Key Parties

Servicer and collection account bank	BPM ('A'/'F1'/Stable)
Account bank, Cash Manager and Principal Paying Agent	HSBC Bank plc ('AA'/'F1+' / Negative)
Rep of Noteholders	HSBC corporate trustee company (UK) Ltd.

Source: Transaction documents

## Counterparty Risk

### The Originator and Servicer

The loans were originated by BPM (rated 'F1'/'A'/Stable Outlook) in its normal course of business prior to being transferred to the issuer.

BPM fulfils the roles of servicer and collection account bank in this transaction. Although structural mitigants are in place, the rated notes could be vulnerable to a sudden default of BPM from its current ratings.

BPM is the eighth-largest bank and fourth-largest cooperative bank in Italy (by end-2007 total assets), with a national share of loans and deposits of around 2%. BPM's asset quality is healthy, with a low proportion of impaired loans and with higher-than-average loan impairment coverage of these loans. However, borrower concentration levels at BPM remain higher than average for a cooperative bank mostly engaged in retail, small business and SME lending, reflecting its strong position in industrial Lombardy. The bank also has a significant presence in other Italian regions including Lazio, Piedmont, Apulia and Emilia Romagna.

In view of BPM's importance in the regions in which it operates, Fitch considers that there is a moderate probability that the bank would be supported by the authorities, should the need arise.

Fitch conducted an on-site review at BPM's premises in November 2008 as part of its analysis of the origination and servicing capabilities of the bank, and deemed BPM's procedures in line with Italian market standards. Please refer to *Appendix B* for more details on the origination and servicing procedures followed by the bank.

### Claw-Back Risk

The assignment of the collateral portfolio executed under this transaction is subject to revocation on bankruptcy under article 67 of the Italian bankruptcy law, in the event that the adjudication of bankruptcy of BPM is made within three months of the purchase of the portfolio. To mitigate this risk for the SPV, BPM has provided: (a) a solvency certificate signed by a duly empowered representative; (b) a certificate of good standing issued by the competent Chamber of Commerce (Camera di Commercio) declaring that no insolvency proceedings are pending against it; and (c) a solvency certificate issued by the competent court declaring that no insolvency proceedings are pending against it. However, note that the portfolio was transferred to the issuer on the first of December 2008; hence, as of the date of publication of this report, the three month period has already expired.

### Set-Off Risk

The underlying obligors have a current account with BPM, and may keep their funds with the bank. In the event of an insolvency of the bank, they may try to set-off any losses suffered on their deposits against amounts they owe to the bank under their loan, creating a risk for noteholders. Compared to other European

### Support Ratings

BPM's Support Rating offers Fitch's view of a third-party's propensity and ability to support the bank.

BPM's current Support Rating of '3' indicates a moderate probability of external support from the state.

The Italian state is highly rated ('F1+'/'AA-'/Stable Outlook') but may not in all scenarios have the capability to support BPM.

Further information on Support Ratings and Support Rating Floors is available on Fitch's web site.

jurisdictions, crystallisation of set-off rights occurs earlier in Italy, as the potential set-off risk is limited to claims of the borrowers towards BPM that have arisen before the later of: (i) the date of publication of the notice of transfer in the Official Gazette; and (ii) the date of registration of the transfer with the companies' registrar. The maximum set-off amount is equal to EUR8.77m as of the closing date; it will progressively be reduced by any withdrawal subsequently made by the relevant borrower. New balances arising as a consequence of subsequent deposits cannot be offset against the issuer. BPM shall provide to Fitch, on a quarterly basis, information in respect of the current account balances held by the relevant borrowers with BPM in order to identify potential set-off amounts. If its Short-Term Rating falls below 'F1', BPM shall deposit into an account opened with an eligible institution in the name of the issuer, cash collateral in an amount equal to the potential set-off amount, as last determined by BPM.

### **Commingling Risk**

The issuer is subject to the risk that, in the event of insolvency of BPM, the collections then held by the servicer are lost. To mitigate such risk, the issuer has the obligation to credit any collections and recoveries to the Transaction Account, held in its name at HSBC Bank plc (rated 'AA'/'F1+'/'Negative, and referred to as the 'account bank') within two days of receipt. Moreover, if BPM is downgraded to 'F3' or below, the relevant borrowers will be promptly notified to pay their instalments directly in the above-mentioned transaction account (see "*Commingling Risk in Structured Finance Transactions: Servicer and Account Bank Criteria*", dated 9 June 2004 and available at [www.fitchratings.com](http://www.fitchratings.com)). Finally, if BPM is downgraded below 'A', the issuer will appoint a back-up servicer.

### **Account Bank and Eligible Investments**

The issuer available funds standing to the credit of the transaction account will be invested on behalf of the issuer in eligible investments, subject to the following conditions (see "*Counterparty Risk in Structured Finance: Qualified Investment Criteria*", dated 27 September 2007 and available at [www.fitchratings.com](http://www.fitchratings.com)):

- they must be denominated in euro;
- they are rated at least 'AA-' and/or 'F1+' for securities and 'AAA' and/or 'V1+' for money market funds; and
- they mature prior to the following payment date, or can be liquidated without penalty before the next payment date.

If HSBC bank plc is downgraded below 'F1', the issuer must find a replacement account bank with a minimum rating of 'F1' within 30 days (see "*Commingling Risk in Structured Finance Transactions: Servicer and Account Bank Criteria*", dated 9 June 2004 and available at [www.fitchratings.com](http://www.fitchratings.com)).

All the above-mentioned mechanisms are in line with Fitch's current criteria for counterparty risk exposure, and are meant to mitigate such risk. However, the class A notes would be vulnerable if there was a sudden and direct default of BPM or HSBC bank. Fitch is currently reviewing its counterparty criteria; for further information please see the 15 October 2008 commentary, entitled, "*Fitch: Counterparty Criteria for Global Structured Finance under Review*", available on the agency's public web site, [www.fitchratings.com](http://www.fitchratings.com).

### **Performance Analytics**

Fitch will monitor the transaction regularly and as warranted by events, with a review conducted at least yearly. Events which may trigger a review include, but are not limited to, the following:

1. asset delinquencies and defaults;

2. portfolio migration (the quarterly servicer report will include loan-by-loan information with regards to, among others, the internal ratings assigned to the obligors by BPM);
3. a counterparty rating downgrade or jump to default.

The surveillance process follows the same two-step process outlined above in the *Asset Analysis* and *Cash Flow Modelling* sections; however, all analysis is conducted on the basis of the then current portfolio. Fitch's 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.

BBS supplied internal credit scores and expected PDs for the obligors in the portfolio. These were reviewed but not relied on in Fitch's quantitative analysis. As mentioned above, Fitch will use this information in its ongoing surveillance of the portfolio.

Details of the transaction's performance are available to subscribers at [www.fitchresearch.com](http://www.fitchresearch.com). Further information on this service is available at [www.fitchratings.com](http://www.fitchratings.com).

Please call the Fitch analysts listed on the first page of this report with any queries regarding the initial analysis or the ongoing surveillance.

**Appendix A: Transaction Comparison**

**Transaction Comparison**

Transaction name	BPM Securitisation 2	UBI Finance 2	PMI 2 Finance	TdA Sa Nostra Empresas 1, FTA
Originator and Servicer	BPM	UBI Banca	Unicredit Banca d'Impresa	Caja de Ahorros y Monte de Piedad de Las Baleares
Closing date	Mar 09	Feb 09	Nov 04	Nov 08
Reinvestment period (years)	n.a.	n.a.	n.a.	n.a.
Principal lock-out period (months)	18	18	18	18
Transaction size (EURm)	1,301.83	2,079.35	307.3	250
Capital structure (% credit enhancement) 'AAA' (class A)	29.4	25.0	11.8	35.4
<b>Portfolio overview</b>	<b>Actual</b>	<b>Actual</b>	<b>Actual</b>	<b>Actual</b>
Number of loans	10,725	8,018	737	830
Number of obligors	9,322	7,190	737	746
Largest obligor (%)	2.8	2.4	0.49	4
Largest 10 obligors (%)	12.1	13.4	3.99	23.5
Fitch weighted average rating factor	B+	BB	BBB-/BB+	BB-/B+
Fitch weighted average recovery rate ('AAA')	24.4	22.7	14.3	52.8
Weighted average coupon on fixed collateral (%)	5.71	5.14	n.a.	5.9
Weighted average margin on float collateral (%)	1.20	1.05	1.52	1.1
Floating rate securities (%)	80.9	86.5	100	92.8
<b>Weighted average life (years)</b>	<b>4</b>	<b>6</b>	<b>2.75</b>	<b>10.6</b>
<b>Portfolio composition (%)</b>				
Mortgage loans	67	61	0	54.1
Unsecured loans	33	39	100	45.9

n.a. - not applicable

Source: Transaction documents and Fitch

## Appendix B: Servicing and Origination

Fitch conducted an on-site review at BPM's premises in November 2008 as part of its analysis of the origination and servicing capabilities of the bank, and deemed BPM's procedures in line with Italian market standards.

### Origination

Loans are always originated at branch level, without recourse to external brokers. The set of documents that must be provided by potential borrowers include:

- if the applicant is the owner of an individual firm or an independent professional, registration in the professional register and/or Chamber of Commerce, accounts and tax documentation relating to the business, as well as relevant information on the business (eg sector performance);
- if the applicant is a company, an updated Chamber of Commerce certificate, income statement and balance sheet for the current financial period, and an updated report on bank guarantees and how they are used.

Moreover, in case of mortgage loans, documents relating to the real estate property must also be provided, eg the land registry certificate.

The risk profile of the potential borrowers is assessed by means of BPM's internal rating system, whereby each borrower is assigned a counterparty rating irrespective of the specific features of the loan applied for. The internal rating reflects the one year default probability and depends on financial, qualitative and behavioural information. Decisions as regards the amount of credit to extend are approved at different levels of BPM's management structure, ranging from branch manager up to the Board of Directors, depending on the size of exposure. Moreover, local branches and other authorities reporting to the bank's commercial division (eg local area managers or SME managers) can approve credit applications within their predefined authority levels provided that:

- the applicant's internal rating is higher than a given threshold; and
- certain 'safety' conditions are met, relating for instance to the LTV (which has to be lower than 50%), mortgage rank (has to be first rank) and loan tenor (within 10 years for mortgage loans and three years for unsecured loans).

Unless these conditions are met, local or central units of the credit division are always responsible for loan approvals. Either way, the maximum loan amount that can be approved by a branch manager is EUR150,000 for mortgage loans or EUR50,000 for unsecured loans. For mortgage loans, the value of commercial properties is estimated by qualified external appraisers or, in case of loan amounts larger than EUR500,000, directly by BPM appraisers. All properties are insured against the risk of fire and explosion.

### BPM Internal Rating System

BPM first developed an internal rating system (IRS) for corporates and SMEs in 2001/2002. After a number of revisions, the bank adopted an entirely new rating system between 2007/2008. No meaningful comparison is possible between the new and the old internal ratings.

The new rating system is based on three separate internal rating scales for small business, SMEs, and corporate borrowers, respectively. For all three types of borrowers the bank's internal rating is based on different modules relating to financial statement analysis, behavioural score, and a qualitative questionnaire (which can change the internal rating by no more than one notch). Rating overrides are possible for SMEs and corporates (not for small business) and can change the ratings by no more than three notches; however, ratings cannot be overridden by employees of the commercial division, only by senior analysts in the credit division. The rating is used in the underwriting process (as it is one of the factors that can prevent the authorisation of the loan at branch level) and for risk monitoring purposes. The IRS accuracy ratio ranges from 70% (corporates) to 79% (SMEs).

### Servicing and Work-out Process

The instalments of all the loans included in the collateral portfolio are paid by direct debit from the obligors' current account. Loans granted before November 2002 pay due instalments every day of the month, while after that date, instalments are due on the last day of the month.

Fifteen days after the first missed instalment the system automatically sends a letter to the client to inform them of their debit position; 15 days later, a second letter is sent to request the payment. Branches receive a printout that highlights every instalment in arrears on a monthly basis.

Delinquent loans are managed by a central department named 'Area Rischi e Gestioni Accentrate' (ARGA). The definition of delinquency implies a period of temporary distress for the borrower, during which, BPM mainly attempts to bring the borrower back to performance. More specifically, a loan is classified as delinquent when the borrower fails to pay one annual or semi-annual instalment for longer than 90 days after the relevant due date (or fails to pay two quarterly instalments or four monthly instalments). Furthermore, a loan is classified as delinquent as soon as there is evidence of negative performance, sourced from the Bank of Italy's central credit register (Centrale Rischi) or from tribunals (in case of protests).

A loan is classified as defaulted when the relevant borrower is believed to be in a state of permanent distress, even if not judicially ascertained. More specifically, a loan is classified as defaulted when the borrower fails to pay one annual instalment for longer than 180 days (or fails to pay two semi-annual instalments or three quarterly instalments or six monthly instalments). If the loan amount is less than EUR50,000, or if insolvency proceedings have commenced, the relationship manager (gestore della posizione) classifies the loan as defaulted; otherwise, the relationship manager transmits the classification proposal to the ARGA department, which carries out its own evaluation and then passes the findings on to the central committee (Comitato di Direzione per il Passaggio a Sofferenza) to make a decision.

Defaulted loans are handled by the bank's Legal Department (55 people), which focuses on achieving out-of-court settlements. Any such settlements are assessed by BPM, mainly on the basis of the mortgaged property's value and the estimated time to recovery. In cases where it is not possible to reach an out-of-court agreement, the legal department will seek an enforcement order against the mortgaged real estate assets.

**Appendix C: Transaction Overview**

**BPM Securitisation 2 S.r.l. - Series 2009-1**

**Italy/SME CDO**

**Capital Structure - Total Issuance EUR1,301.83m**

Class	Rating <sup>b</sup>	Size (EURm)	CE (%) <sup>a</sup>	PMT freq	Basis	Spread coupon (%)	First IPD	Maturity	ISIN
A	AAA	923.95	29.4	Semi-annual	EUR6m	1.00	July 09	April 41	
B	NR	377.88		Semi-annual	EUR6m	4.00	July 09	April 41	

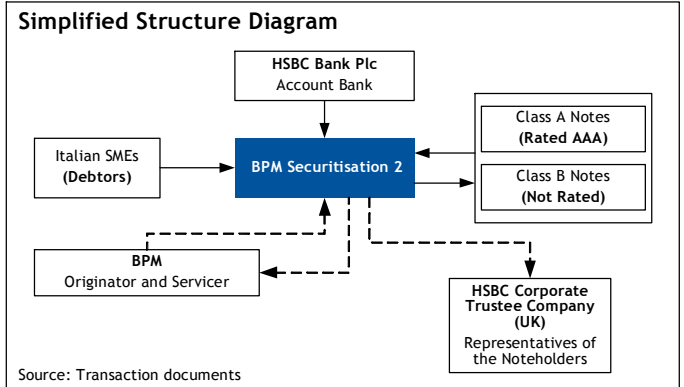
<sup>a</sup> Credit enhancement in the form of subordination only (calculated on a portfolio of EUR1,285.1m)  
<sup>b</sup> The rating assigned to class A notes addresses timely payment of interest and ultimate payment of principal.

**Key Information**

<b>Purpose</b>	Balance sheet	<b>Role</b>	Party (trigger)
<b>Location of assets</b>	Italy	<b>Servicer and Collection Account Bank</b>	BPM ('F1')
<b>Structure</b>	Pass-through, sequential	<b>Account bank</b>	HSBC Bank plc ('F1')
<b>Credit enhancement type</b>	Overcollateralisation, excess spread	<b>Cash Manager and Principal Paying Agent</b>	HSBC Bank plc ('F1')
<b>Portfolio composition</b>	Primarily Italian senior secured loans	<b>Issuer</b>	BPM Securitisation 2 S.r.l.
<b>Location of SPV</b>	Italy	<b>Trustee</b>	HSBC Corporate Trustee Company (UK) Ltd
<b>Primary analyst</b>	alessandro.cipolla@fitchratings.com		
<b>Performance analyst</b>	jeffery.cromartie@fitchratings.com		

**Structural Information**

Closing date	26 March 2009
Principal lock-out period (months)	18
Reinvestment period	n.a.



**Key Rating Drivers**

- Defaults, Recovery Rates & Correlation:** the key drivers behind the ratings are the assumptions for the expected levels of defaults, recovery rates, and the correlation such a pool would exhibit. Fitch's assumptions for each of these are highlighted in this report and the sensitivity to these drivers is covered within the *Rating Sensitivity* section. For example, increasing the probability of default (PD) of each loan in the PCM by a factor of 25%, using a relative haircut of the tiered asset-specific recovery rate of 50%, and increasing the industry correlation by 10% (*Severe Stress*), results in a model-implied five notch downgrade of class A from 'AAA' to 'A'. However, actual rating volatility may be different to model-implied rating volatility, as multiple variables may shift differently from that which has been assumed.
- Industry Concentration:** the largest industry is real estate and accounts for about 43% of the portfolio notional. Real estate concentration has been accounted for in Fitch's analysis by the assumed correlation level and by stress-testing the rating for shocks in the assumed portfolio default rates (please refer to the *Rating Sensitivity* section above for more details).
- Single Obligor Concentration:** the largest 10 obligors represent 12.1% of the total portfolio. Fitch performed credit assessments on the largest 19 exposures, accounting for about 17% of the portfolio notional. Additionally, the class A notes have sufficient subordination to withstand the estimated default of the largest 10 obligors (see *Transaction Summary* and *Portfolio Stratification* sections).
- No Hedging Agreement:** no interest rate hedging agreement has been put in place for this transaction, leaving the SPV exposed to interest rate basis and reset risk; this has been taken into account in Fitch's cash flow analysis of the transaction (refer to the *Cash Flow Modelling* section above for more details).
- Counterparty risk relating to the collection account bank and the account bank:** BPM and HSBC fulfil the roles of collection account bank and account bank respectively. The resulting counterparty risk is mitigated by their current ratings and by structural mitigants envisaging the replacement of the guarantor following its downgrade below 'F1'. However, the transaction would be exposed to a sudden jump to default of these institutions from their current rating.

Source: Fitch and Transaction documents.

Copyright © 2009 by Fitch, Inc., Fitch Ratings Ltd. and its subsidiaries. One State Street Plaza, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. All of the information contained herein is based on information obtained from issuers, other obligors, underwriters, and other sources which Fitch believes to be reliable. Fitch does not audit or verify the truth or accuracy of any such information. As a result, the information in this report is provided "as is" without any representation or warranty of any kind. A Fitch rating is an opinion as to the creditworthiness of a security. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed, suspended, or withdrawn at anytime for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of Great Britain, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.