

European Securitized Products Weekly

The Knock-On Effect to Continue

- **Possible FLS Extension to Sustain Strong Technicals** — The possible extension of the Bank of England's FLS scheme beyond January 2014 (as reported by Financial Times) should sustain the already favourable technicals in the European securitized space. UK prime scarcity continues to drive investors to other high quality sectors, causing a knock-on effect of spread tightening in these sectors. We expect Dutch RMBS, UK BTL RMBS, and German multi-family CMBS to benefit most from this effect.
- **Peripherals Offer Better Entry Points** — We advise taking advantage of better entry points after last month's widening for adding exposure to select high quality peripheral sectors. Italian RMBS widened 40bp to EURIBOR +239bp and Spanish and Irish RMBS widened 20bp each to +285 and +330bp, respectively, following the inconclusive Italian elections. We like Italian RMBS because of strong fundamentals and think many first-pay Spanish SME ABS also offer good value.
- **First Tender of 2013 to Boost Sentiment** — The recent launch of a €1.6 billion tender offer for Spanish RMBS and SME ABS by Cajamar Caja Rural indicates the possibility of more peripheral tenders in 2013. Although the final take-up and execution prices of the tender are yet to be seen, the likelihood of future tenders would boost investor sentiment.

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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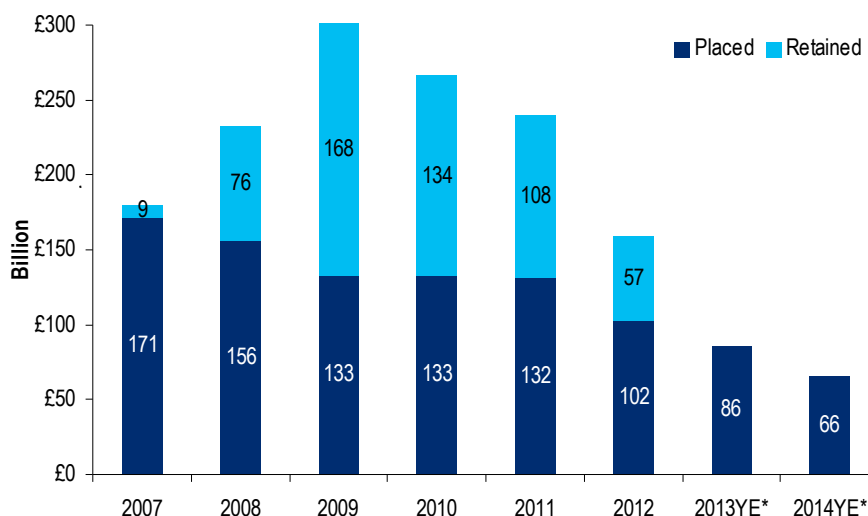
Survey of Relative Value

Favourable Technicals to Persist

Possible FLS extension could sustain the strong technical bid.

We expect that favourable technicals due to lack of primary supply will continue to support core sector spreads in 2013. Total placed issuance in 2013 YTD registers €11 billion, roughly 28% lower than the comparable period in 2012 and the pipeline remains thin. UK RMBS primary market has been totally shut off because of the Bank of England's ongoing Funding for Lending Scheme (FLS), which provides UK lenders more attractive funding than securitized markets. The FLS is likely to extend beyond the original January 2014 deadline, according to a recent article in the Financial Times.¹ Until now the market was expecting UK prime issuance to re-start in 2013 H2 before the end of FLS drawdown period. However, the FLS extension would impact new issuance beyond 2013 and force investors to look to alternative sectors. We estimate that the size of placed UK prime RMBS market will decrease to £66 billion by 2014 year-end in absence of new issue supply. This equates to a 62% decrease from the peak of around £171 billion outstanding in 2007 (Figure 1).

Figure 1. Estimated Runoff of UK Prime RMBS Universe, 2007 – 2012 and 2013 – 2014 Est. (£ billion)



*The numbers are based on the assumption of no new issuance in 2013 and 2014. We do not project retained outstanding.

Source: Investor Reports, Concept ABS Bloomberg, and Citi Research

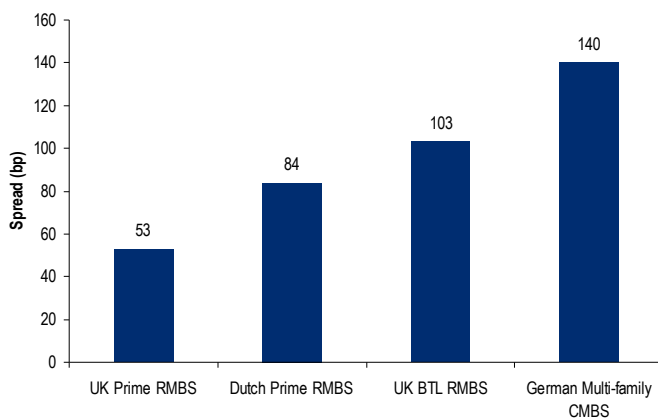
Attractive UK Prime Alternatives

We think that the prolonged scarcity and tight spreads of UK prime paper will continue to trigger a chain reaction of spread tightening in other substitute sectors as investors look for suitable alternatives. Dutch RMBS, UK buy-to-let, and German multi-family CMBS would benefit most from this effect, in our opinion. These sectors are apparent UK prime substitutes offering good quality core country residential exposure and attractive pickups to UK prime RMBS (Figure 2). Although these sectors have so far lagged the significant UK prime rally since the August 2012 FLS announcement, the dearth of UK prime paper for an extended period would continue to drive investors to these sectors, creating attractive technicals.

¹ [Funding for Lending to be 'put on steroids'](#), Financial Times, 11 March 2013

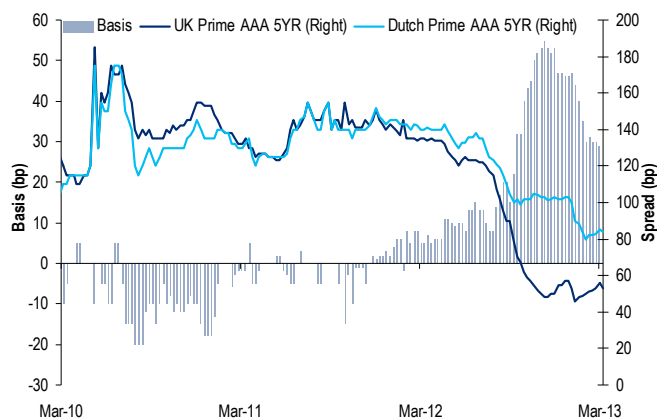
- **Dutch and UK Prime RMBS Basis Unusually High.** The 29bp differential between Triple-A rated 5YR Dutch and UK Prime RMBS is wide compared to historical levels (Figure 3). UK prime rallied from 107bp to 53bp since August 2012. While the Dutch RMBS has rallied considerably in January, narrowing the gap from 46bp to 29bp, we think that Dutch spreads could tighten further.

Figure 2. Spread Comparison of Select High Quality UK Prime Alternatives, as of 8 March 2013 (bp)



Source: Citi Research

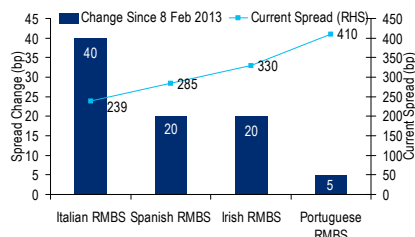
Figure 3. Dutch and UK Prime RMBS Spread Differential, Mar 10 – Mar 13 (bp)



Source: Citi Research

Better Entry Points for Peripherals

Figure 4. Peripheral RMBS Spread Widening Since 8 Feb 2013, as of 15 March 2013 (bp)



Source: Citi Research

Peripheral RMBS sectors look attractive again after last month's widening, following inconclusive Italian elections and UK and Italy sovereign downgrades. For instance, senior Italian RMBS widened 40bp to EURIBOR +239bp and Spanish and Irish RMBS widened 20bp each to +285bp and +330bp, respectively, since 8 February 2013 (Figure 4). Some spread consolidation was expected following the impressive January rally as highlighted in our previous "Survey of Relative Value."² The political uncertainty and sovereign downgrades triggered the correction affecting peripheral securitized markets the most. In contrast, UK and Dutch Prime RMBS widened only 2bp to EURIBOR +53bp and +84bp, respectively, proving resilient in the face of macro uncertainties.

We now recommend investors take advantage of better entry points for adding exposure to select high quality peripheral sectors. Italian RMBS is one of our top picks for 2013 and we also like certain first-pay and fast amortizing Spanish SME ABS.³ Italian mortgage market fundamentals are the strongest among peripheral countries because of low indebtedness of Italian households and relatively stable house prices.

Recent positive news from peripheral countries should help improve investor sentiment. First, the €1.6 billion tender announcement by Cajamar Caja Rural for their IMCAJ 1, IMCAJ 2, IMCAJ 3, TDCAJ 2, and IMCEM 2008-2 RMBS and SME ABS programmes is very positive for the Spanish sector. The possibility of further tenders from peripheral banks would provide strong technical support to peripheral spreads.

Spanish tender announcement and successful Irish government bond auction to boost sentiment.

² "European Securitized Products Weekly: Distinguishing Values along the Credit Spread Curves", Citi, 8 February 2013

³ "European Securitized Products Weekly: An Overview of Spanish SME ABS", Citi, 22 February 2013

In another positive development, the National Treasury Management Agency (NTMA) of Ireland successfully raised €5 billion through the sale of a new 10YR Treasury bond after a gap of more than three years. The issue was 2.6 times over-subscribed and priced at a yield of 4.15%. The fact that around 82% of the issue was taken by international investors highlights the growing appetite of peripheral assets in international debt markets.

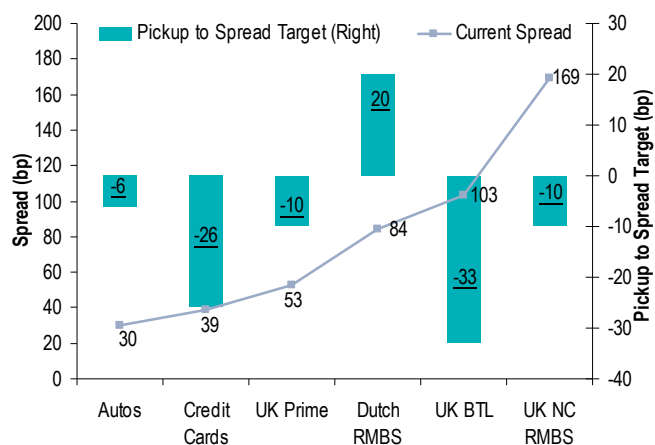
Relative Value Framework

Most core country securitized spreads are expensive to historical averages but they are cheap compared to the US counterparts. European autos and credit cards pick up 27–29bp to comparable US sectors and European CMBS also looks cheap to US CMBS. On the other hand, peripheral RMBS still look attractive compared to our long term spread targets.

Pickups to Spread Targets

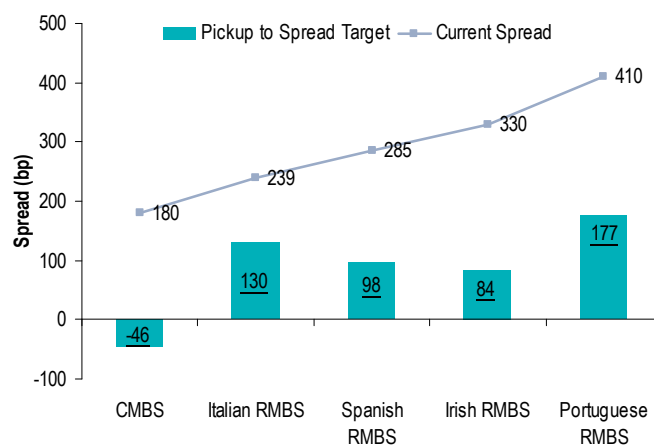
- **Dutch RMBS Attractive.** At EURBOR +84bp, senior Dutch RMBS picks up 20bp to our long term spread target. Dutch RMBS is the only core sector that remains cheap to our spread target while all other core securitized sectors are trading 6–33bp tighter than our spread targets (Figure 5).
- **UK NC RMBS Fairly Valued.** Although UK non-conforming RMBS trades 10bp tight to long-term adjusted mean spreads, we think it is fairly valued because other UK RMBS sectors trade well inside the historical averages (Figure 5). Current spreads for senior UK non-conforming RMBS are LIBOR +169bp.
- **Peripheral RMBS Remain Cheap.** Peripheral RMBS sectors continue to offer attractive pickups to our long term spread targets. Italian, Spanish, Irish, and Portuguese RMBS trade 130bp, 98bp, 84bp, and 177bp wide respectively to historical averages (Figure 6).

Figure 5. Core Sectors Spread Pickup to Spread Targets, as of 8 Mar 2013 (bp)



Source: Citi Research

Figure 6. CMBS and Peripheral Sectors Spread Pickup to Spread Targets, as of 8 Mar 2013 (bp)

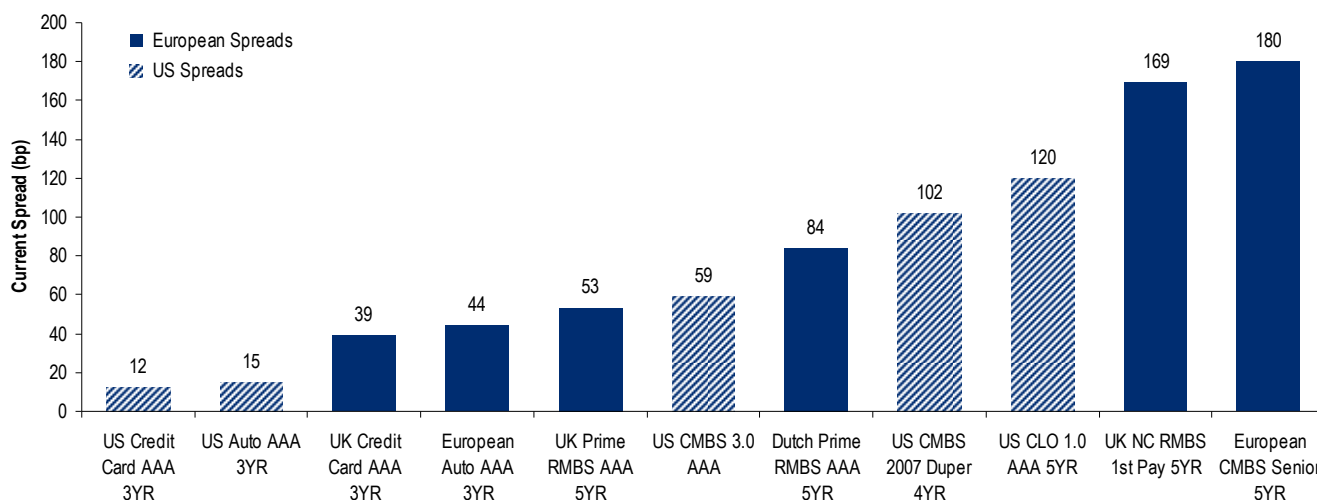


Source: Citi Research

European Securitized Attractive to US

- **European CMBS and UK NC Cheaper than US CMBS and CLO.** European CMBS at EURIBOR+180bp and UK non conforming RMBS at LIBOR +169bp offer attractive pickup to US CMBS 2007 Duper at SWAPS +102bp and US CLO 1.0 at LIBOR +120bp (Figure 7).
- **Autos and Credit Cards Cheap to US Counterparts.** 3YR European autos (EURIBOR +44bp) and 3YR UK credit cards (EURIBOR +39bp) have weathered the recent widening well and still remain very attractive compared to US autos (SWAPS +15bp) and credit cards (SWAPS +12bp).

Figure 7. Selected Securitized Product Spreads to SWAPS, LIBOR and EURIBOR Comparisons, as of 8 Mar 2013 (bp)



Source: Citi Research

Summary of Recommendations

We outline our recommendations below in Figure 8.

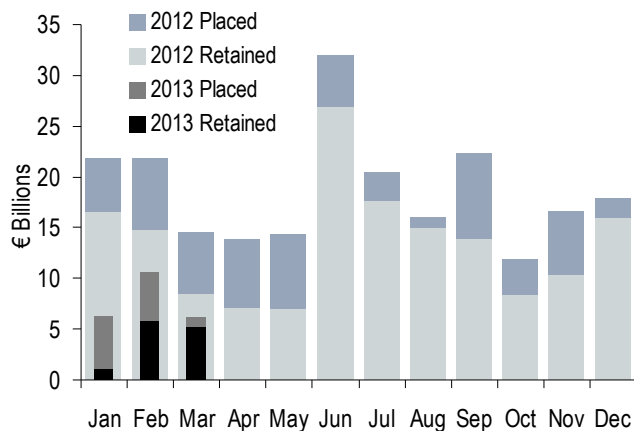
Figure 8. European Securitized Products Sector Recommendations

Category	Sector	Senior	Subordinate	Comments
Top Calls	Italian RMBS	Overweight	Overweight	Low LTVs, relatively low house price declines, and positive net mortgage lending Short WAL, attractive pickup to comparable US credit cards with equivalent credit performance Strong fundamentals like rising rents and falling homeownership, supported by low interest rates
	UK Credit Cards	Overweight	Overweight	
	UK BTL RMBS	Overweight	Overweight	
Core	UK Prime RMBS	Marketweight	Marketweight	Favourable technicals to support spreads
	UK NCRMBS	Marketweight	Underweight	Credit performance likely to deteriorate fast when interest rates rise but we think seniors are well protected
	Dutch RMBS	Marketweight	Underweight	Falling house prices and rising unemployment a concern but strong demand for core RMBS a positive
	Australian RMBS Autos	Overweight	Overweight	Credit performance better than UK prime RMBS, low doc loans potential concern for subordinates Short duration, high quality. Very few comparable short and high quality credit alternatives to this sector
Peripherals	Irish RMBS	Marketweight	Underweight	Very high indexed LTVs to impact subordinate recoveries but tender likelihood to support spreads No major housing boom but high unemployment and negative economic growth outlook a concern Further house price drop likely but bad bank plan and possibility of tenders overall positive for the sector
	Portuguese RMBS	Marketweight	Underweight	
	Spanish RMBS	Marketweight	Underweight	
Other	CMBS	Marketweight	Underweight	Seniors are protected but a large maturity pipeline in 2013 and beyond to impact recoveries This sector requires in-depth bespoke corporate analysis
	Pubs	Underweight	Underweight	

Source: Citi Research

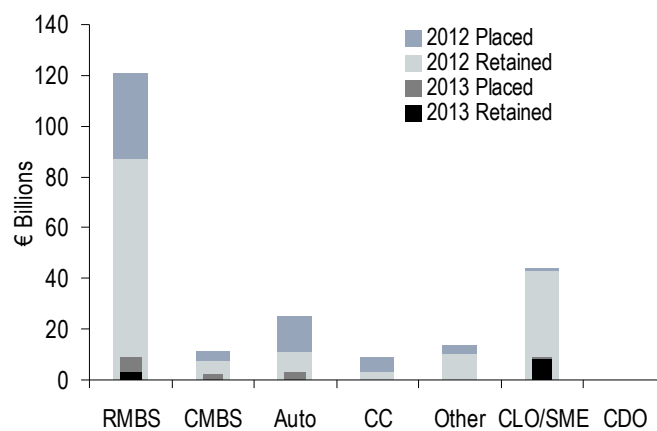
New Issuance

Figure 9. Placed and Retained Issuance by Month, 2012–2013YTD (€ billions)



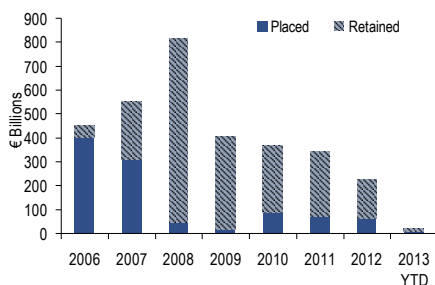
Source: Concept ABS, IFR, Informa and Citi Research

Figure 10. Placed and Retained Issuance by Sector, 2012–2013YTD (€ billions)



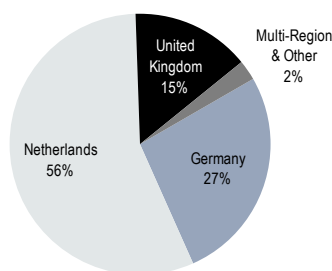
Source: Concept ABS, IFR, Informa and Citi Research

Figure 11. Annual Historical Placed and Retained Issuance, 2006–2013YTD (€ billions)



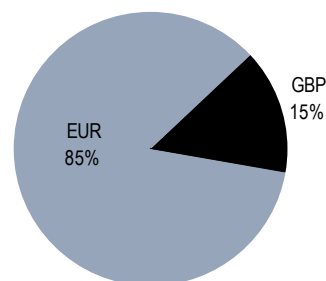
Source: Concept ABS, IFR, Informa and Citi Research

Figure 12. Placed Issuance by Region, 2013YTD (% of Total, € Equivalent)



Source: Concept ABS, IFR, Informa and Citi Research

Figure 13. Placed Issuance by Currency, 2013YTD (% of Total, € Equivalent)



Source: Concept ABS, IFR, Informa and Citi Research

Figure 14. Placed and Retained Issuance by Sector, 2012* and 2013YTD (€ million)

	RMBS(MM)		CMBS*(MM)		Autos(MM)		Credit Card ABS(MM)		CLO/SME(MM)		Other(MM)		Total(MM)	
	2013YTD	2012	2013YTD	2012	2013YTD	2012	2013YTD	2012	2013YTD	2012	2013YTD	2012	2013YTD	2012
Placed	5,565	33,928	2,387	3,936	2,661	13,921	0	5,591	241	990	0	3,459	10,854	61,825
Retained	3,178	87,137	143	7,460	168	11,364	0	3,067	8,548	42,879	152	10,145	12,188	162,052
Total	8,743	121,065	2,530	11,395	2,830	25,285	0	8,658	8,788	43,869	152	13,604	23,042	223,877

* 2012 complete year

Source: Concept ABS, IFR, Informa and Citi Research

Figure 15. Recent Placed Issuance, 1 Jan — 15 Mar 2013

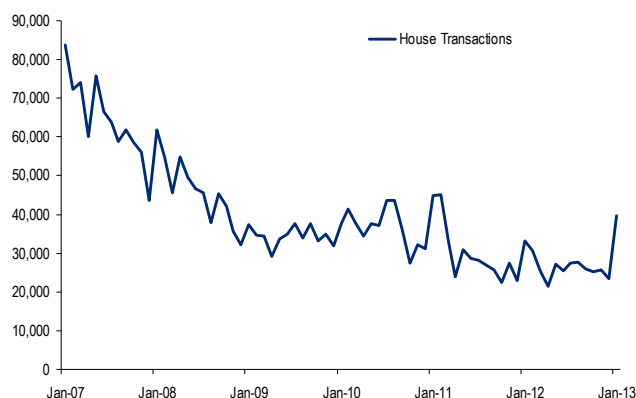
Deal Name	BBG	Transaction Type	Tranche	Currency	Size(MM)	Fitch/Moodys/S&P/DBRS	WAL	Index	Margin	CE	Closing Date
Intu (SGS) Finance plc	-	CMBS - Single Usage Collateral	Series 1 10yr	GBP	450	-/-A/-	10YR	UKT4/22	210 bps		8-Mar
		UK	Series 1 15yr	GBP	350	-/-A/-	15YR	UKT6/28	205 bps		
E-Carat SA Compartment 5	ECAR 2013-1	Auto ABS Germany	A	EUR	500	AAA/-AAA/-	1.64YR	MidSwaps	61bp	12.40%	22-Feb
			B	EUR	30.6	AA/-AA/-	3.33YR	MidSwaps	100bp	6.90%	
			Sub loan	EUR	27.9	NR/-NR/-	N/A	N/A	N/A	0.00%	
VCL Multi-Compartment SA Comp VCL 17	VCL 17	Auto ABS Germany	A	EUR	697.5	-/Aaa/AAA/-	1.29YR	1mE	25bp	8.20%	21-Feb
			B	EUR	21	-/A1/A+/-	1.88YR	1mE	75bp	5.40%	
Arqiva Financing plc	-	CMBS - Business Risk	2013-1a	GBP	350	BBB/-BBB/-	7.3YR		4.04% (Fixed)		21-Feb
		UK	2013-1b	GBP	400	BBB/-BBB/-	12.6YR		4.88% (Fixed)		
Cairn CLO III	CRNCL 2013-3	CLO - Arbitrage Multi Region-Europe	A	EUR	181.5	-/Aaa/ AAA/-		6mE	140bp		20-Feb
			B	EUR	28	-/Aa2/ NR/-		6mE	235bp		
			C	EUR	20	-/A2/ NR/-		6mE	325bp		
			D	EUR	11	-/Baa2/ NR/-		6mE	425bp		
			M	EUR	60	-/NR/ NR/-					
Orange Lion 2013-9 BV	ORANL 2013-9	RMBS - Prime Netherlands	A	EUR	1365	AAA/ Aaa/-/-	5.1YR	3mE	85bp	7.50%	20-Feb
			B	EUR	64.97	NR/ NR/-/-	6YR	N/A	N/A	0.00%	
			C	EUR	42.9	NR/ NR/-/-	6YR	N/A	N/A	0.00%	
Tesco Property Finance 6 plc	-	CMBS - Business Risk - UK	A	GBP	493.4	A-/Baa1/A/-/-	21.1YR	UKT4Q32	245bp	-	7-Feb
Red & Black TME Germany 1 UG	RNBGT 1	Auto ABS Germany	A	EUR	513	AAA/-AAA/-	1YR	1mE	50bp	15.50%	6-Feb
			B	EUR	87	NR/-NR/-	2.8YR	N/A	N/A	1.00%	
Dutch MBS XVIII BV	DUTCH 2013-18	RMBS - Prime Netherlands	A1	EUR	140	AAA/Aaa/-/-	1.96YR	3mE	45bp	5.50%	24-Jan
			A2	EUR	360	AAA/Aaa/-/-	4.96YR	3mE	95bp	5.50%	
			B	EUR	8	AA/Aa2/-/-	5YR	3mE	200bp	4.00%	
			C	EUR	7	A/A2/-/-	5YR	3mE	225bp	2.70%	
			D	EUR	7	BBB/Baa2/-/-	5YR	3mE	250bp	1.70%	
			E	EUR	4.5	B/Ba2/-/-	5YR	3mE	275bp	0.50%	
			F	EUR	2.7	NR/NR/-/-	0.7YR	3mE	300bp	0.00%	
Storm 2013-I BV	STORM 2013-1	RMBS - Prime Netherlands	A1	EUR	150	AAA/ Aaa/ AAA/-	2YR	3mE	45bp	7.00%	22-Jan
			A2	EUR	550	AAA/ Aaa/ AAA/-	4.9YR	3mE	85bp	7.00%	
			B	EUR	17.1	AA-/ Aa1/ AA/-	4.9YR	3mE		4.70%	
			C	EUR	13.1	BBB+/ Aa3/ A/-	4.9YR	3mE		3.00%	
			D	EUR	14.5	BB/ A2/ BBB/-	4.9YR	3mE		1.00%	
			E	EUR	7.5	BB/ Baa3/ NR/-	4.9YR	3mE		0.00%	
Orange Lion 2013-8 BV	ORANL 2013-8	Netherlands RMBS - Prime	A	EUR	3000	AAA/Aaa/-/-	5.1YR	3mE	115bp	9.00%	15-Jan
			B	EUR	191.5	NR/NR/-/-	6YR	Zero	Cpn	0.00%	
			C	EUR	95.7	NR/NR/-/-	6YR	Zero	Cpn	0.00%	

Source: Concept ABS, IFR, Informa and Citi Research

Collateral and Macro Trends

Spain

Figure 16. Spanish House Transactions, Jan 07 – Jan 13

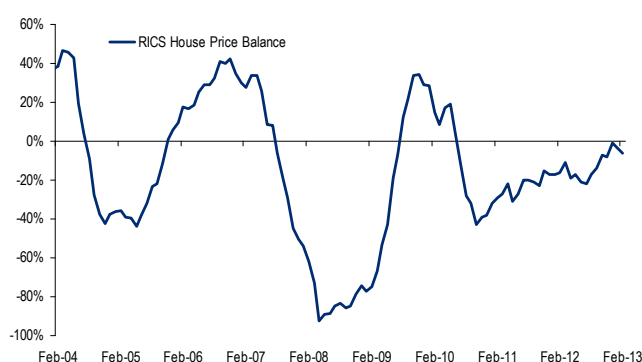


Source: INE

- Spanish house transactions increased to 39,670 in January from 23,523 in the previous month
- House transactions increased 68% month-over-month and 20% year-over-year in January 2013

UK

Figure 17. RICS House Price Balance, Feb 04 – Feb 13

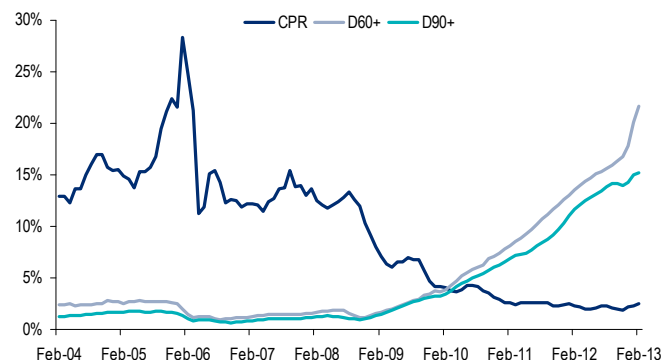


Source: ABSNet and Citi Research

- RICS house price balance declined to -6% in February from -4% in the previous month
- RICS house price balance improved 10 percentage points year-over-year in February

Ireland

Figure 18. Irish RMBS CPR and Delinquencies, Feb 04 – Feb 13

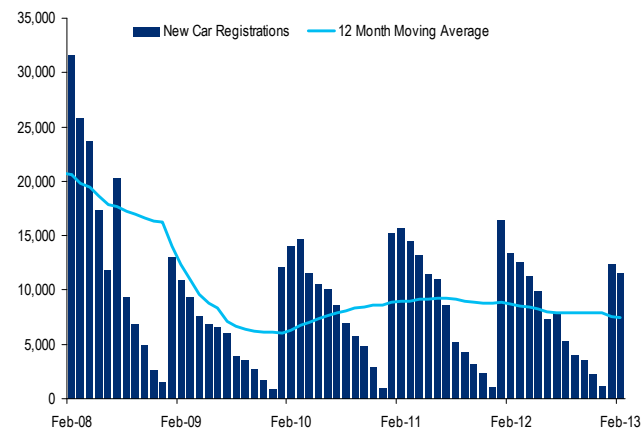


Source: ABSNet and Citi Research

- Irish RMBS 60 day+ delinquencies touched a new high of 21.6% in February and have increased 3.8 percentage points in the past three months
- Irish RMBS CPR rose to 2.4% in February from 2.2% in the previous month

Ireland

Figure 19. New Vehicle Registrations, Feb 08 – Feb 13

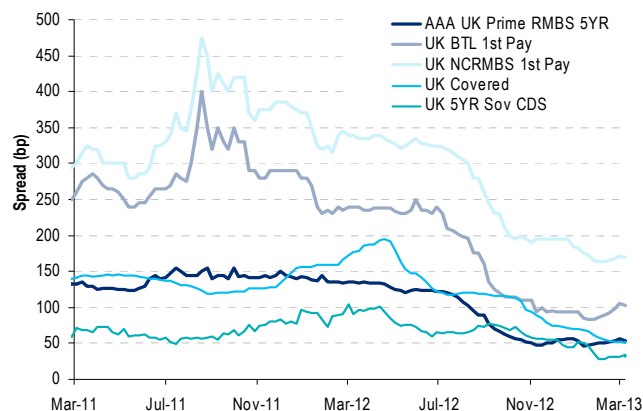


Source: CSO Ireland

- New vehicle registrations fell to 11,518 in February from 12,316 in the previous month
- 12 month moving average of new vehicle registrations fell to 7,428 in February and is down 14.8% year-over-year

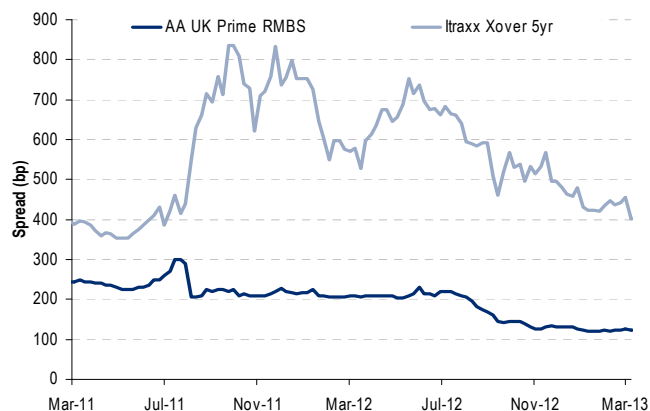
Relative Value Charts

Figure 20. UK RMBS Seniors Versus Indexes, Mar 11 – Mar 13



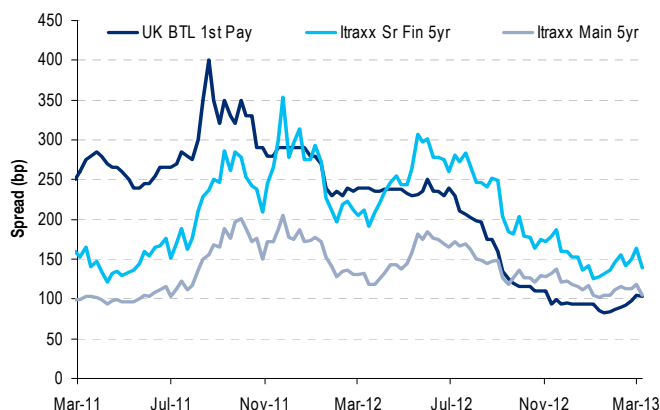
Source: Markit and Citi Research

Figure 21. UK Prime RMBS Subordinates Versus Index, Mar 11 – Mar 13



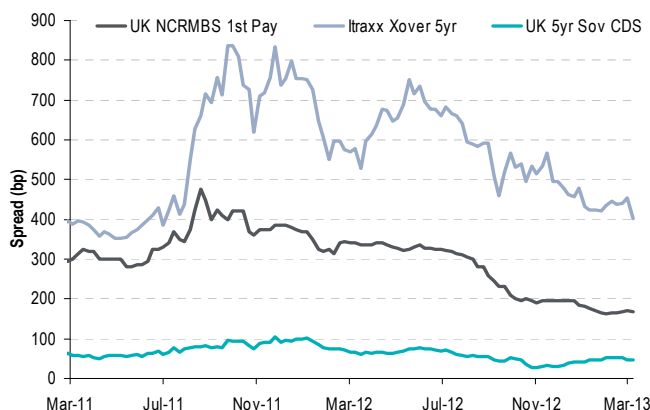
Source: Markit and Citi Research

Figure 22. UK BTL RMBS Seniors Versus Indexes, Mar 11 – Mar 13



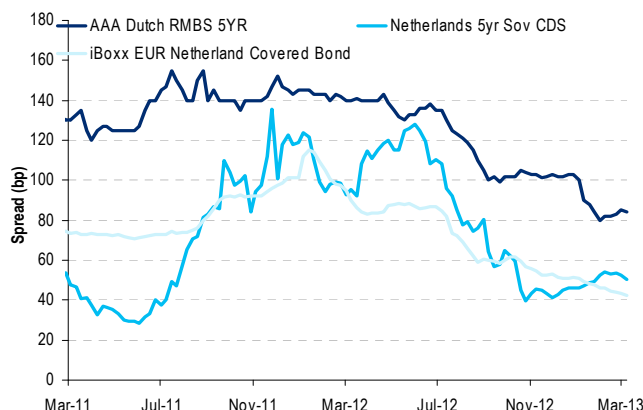
Source: Markit and Citi Research

Figure 23. UK NCRMBS Seniors Versus Indexes, Mar 11 – Mar 13



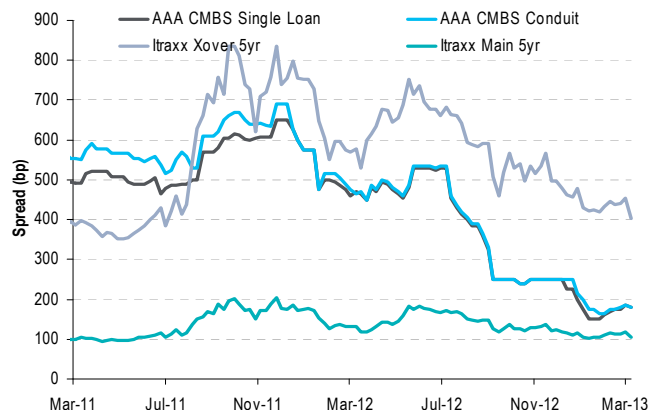
Source: Markit and Citi Research

Figure 24. Dutch RMBS Seniors Versus Indexes, Mar 11 – Mar 13



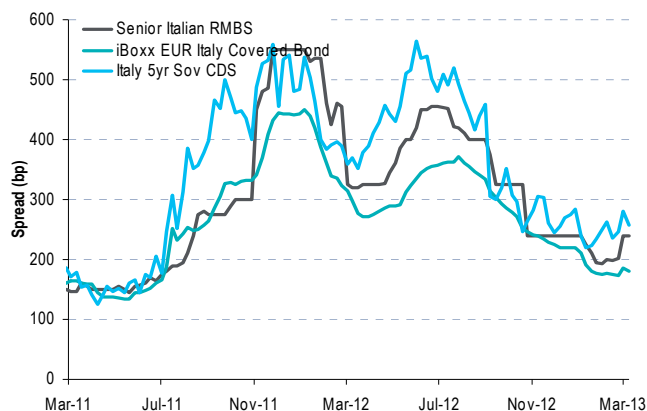
Source: Markit and Citi Research

Figure 25. CMBS Senior Spreads Versus Indexes, Mar 11 – Mar 13



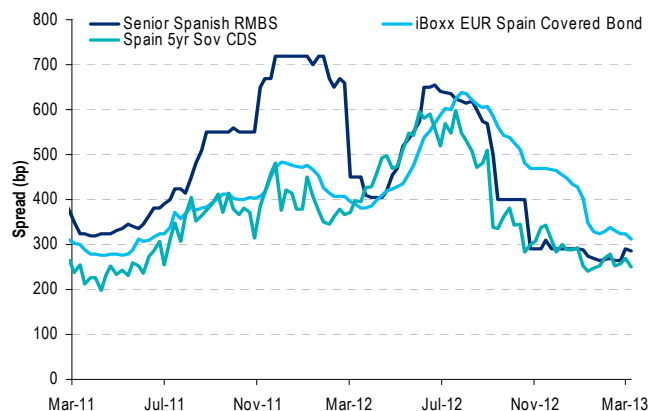
Source: Markit and Citi Research

Figure 26. Italian RMBS Seniors Versus Indexes, Mar 11 – Mar 13



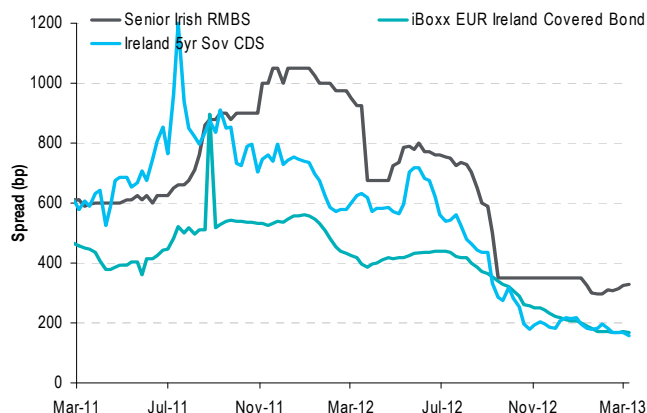
Source: Markit and Citi Research

Figure 27. Spanish RMBS Seniors Versus Indexes, Mar 11 – Mar 13



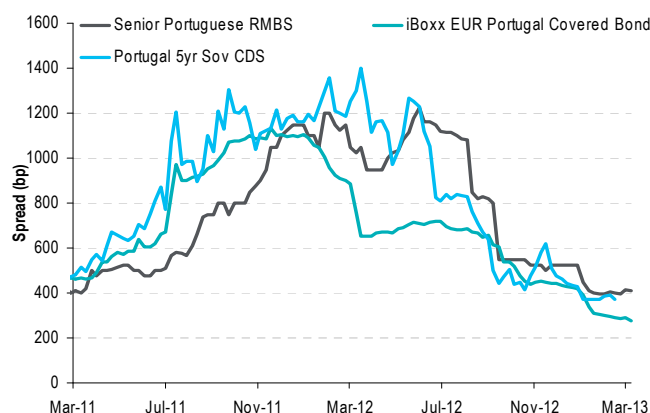
Source: Markit and Citi Research

Figure 28. Irish RMBS Seniors Versus Indexes, Mar 11 – Mar 13



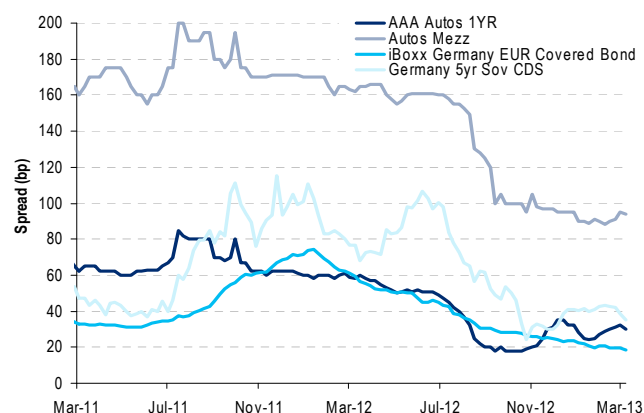
Source: Markit and Citi Research

Figure 29. Portuguese RMBS Seniors Versus Indexes, Mar 11 – Mar 13



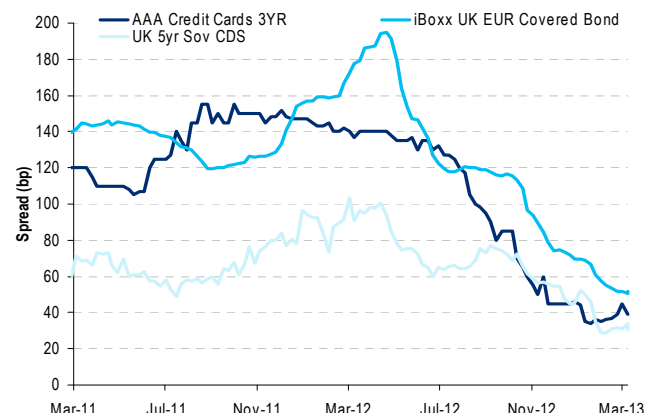
Source: Markit and Citi Research

Figure 30. Auto ABS Spreads Versus Indexes, Mar 11 – Mar 13



Source: Markit and Citi Research

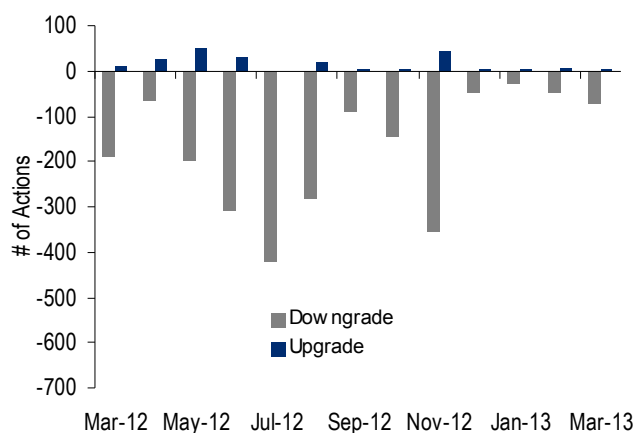
Figure 31. Credit Card ABS Spreads Versus Indexes, Mar 11 – Mar 13



Source: Markit and Citi Research

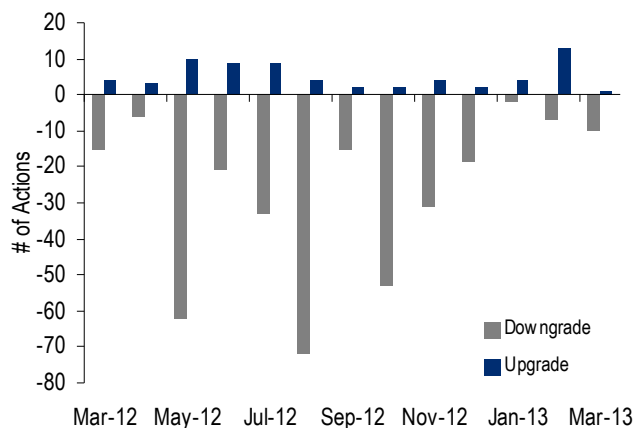
Rating Actions and Trends

Figure 32. European RMBS Rating Actions, Mar 12 – Mar 13



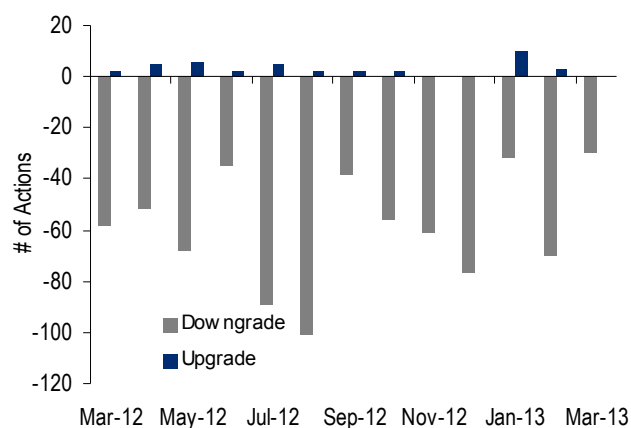
Source: Moody's, S&P and Fitch

Figure 34. European ABS Rating Actions, Mar 12 – Mar 13



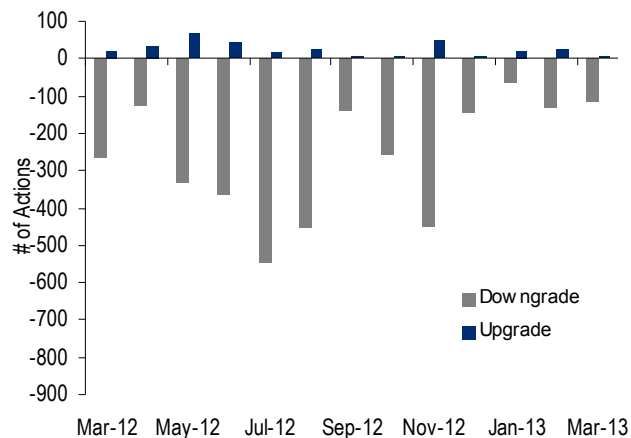
Source: Moody's, S&P and Fitch

Figure 33. European CMBS Rating Actions, Mar 12 – Mar 13



Source: Moody's, S&P and Fitch

Figure 35. European Total Securitized Products Rating Actions, Mar 12 – Mar 13



Source: Moody's, S&P and Fitch

Appendix A-1

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